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No. 11971

United States
Circuit Court of Appeals
for the Ninth Circuit

CECIL E. HUMPHRIES,

Appellant,

vs.

ROBERT A. HEINZE, Warden, etc.,

Appellee.

Transcript of Record

Upon Appeal from the District Court of the United States
for the Northern District of California,
Northern Division

FILED

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AUG 3 - 1948

PAUL P. O'BRIEN.

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Circuit Court of Appeals
for the Ninth Circuit

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NAMES AND ADDRESSES OF ATTORNEYS

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Box No. A-6859,

Represa, Calif.

Attorney for Appellee:

THE ATTORNEY GENERAL,

State of California,

Sacramento, Calif.

In the United States District Court for the
Northern District of California, Sacramento,
California

No. 5981

In the Matter of Application of
CECIL E. HUMPHRIES,
for a Writ of Habeas Corpus.

PETITION FOR WRIT OF HABEAS CORPUS

To the Honorable Dal M. Lemmon, Presiding Judge
of the United States District Court,

Greetings:

The petition of Cecil E. Humphries, for a writ
of Habeas Corpus, respectfully represents and
shows to this Hon. Court:

I.

That your petitioner, Cecil E. Humphries, a
natural born citizen of the United States, over the
age of twenty-one years, is now illegally and unlaw-
fully imprisoned, confined, restrained and deprived
of his lawful right to liberty, by the State of Cali-
fornia, and by Robert A. Heinze, et al., by impris-
onment in the State Prison of the State of Cali-
fornia, contrary to and in violation of the privileges
and immunities, due process of the law, and equal
protection of the laws clauses of Article XIV, Sec-

tion 1, of the Amendment to the Federal Constitution, for reasons immediately hereinafter made to appear:

II.

That prior to the date of the filing of this petition and on July 15, 1947, in Department "B" of the Superior Court of and for the County of Los Angeles, State of California in Santa Monica, before the Hon. Orlando H. Rhodes, judge therein presiding, upon an information, theretofore filed in said Court by the district attorney of the County and State aforesaid, charging petit theft with prior conviction of a felony, being No. 113274.

III.

That the imprisonment of said petitioner, Cecil E. Humphries, is contrary to and in violation of the said privileges and immunities due process of the law, and equal protection of the laws clauses and provisions of the Fourteenth Amendment to the Constitution of the United States of America, and Article 1, Section 13 of the Constitution of the State of California.

The clause XIV, Amendment to the Constitution of the United States which forbids a state to "deny to persons within its jurisdiction the equal protection of the laws."

IV.

Your petitioner, Cecil E. Humphries, contends that he has not had the required protection that is provided for by the Equal protection of the Laws; that the arrest, confinement, conviction and imprisonment is illegal, and the proceedings are likewise

illegal in their entirety; and the trial that was held before the Hon. Orlando H. Rhodes, was unconstitutional wherein the said jury returned its verdict of not guilty, but, because the foreman of the said jury failed to sign his name to the verdict, the Court would not recognize said verdict, and returned the jury for another.

V.

Further, this same jury, acting on the same evidence and charge, and only one court of theft, returned two other verdicts, which was plainly shown double jeopardy.

VI.

Let it be said at this time that the jury took the case for consideration, and at no time was any defense offered in opposition to the pretended evidence, whereas the defense rested without contesting what was supposed to be a case.

VII.

Your petitioner contends that every right that was favorable to him, from the time of arrest, was denied; and an examination of the record in this case will verify and substantiate aforesaid contentions. Whereas your petitioner has been without sufficient funds, only part of the transcript could be obtained, and petitioner, Cecil E. Humphries, beg this Hon. Court to obtain a complete transcript of the said trial, and he do contend that said transcript is sufficient to prove double jeopardy and all other claims which will present a light of truth to all allegations made by petitioner of said case, being No. 113274.

VIII.

That in a writ of Error Coram Nobis to this same judge Orlando H. Rhodes, it was outlined, that according to the California Penal Code, S-1097, that when a reasonable doubt as to the degree, a defendant can be convicted only of the lowest degree, and included, was a case from California reports, Tuttle-1874 No. 4,167, this writ of Coram Nobis was denied; and it is the contention of petitioner that there is not a grand jury in existence in the United States that would bring in an indictment on such evidence as was offered in the conviction in the instant case. Where the present methods are used, as in the present case, your petitioner contends that judge Orlando H. Rhodes, in this case, does not recognize either the constitution of California or the United States, therefore it is absolutely impossible to get a fair and impartial trial in his Court.

IX.

Therefore, wishing to show the allegations of the *none legallity* of the proceedings, petitioner, has a copy of the proceedings at the preliminary hearing.

That on May 7, 1947, the proceeding at this said hearing, plainly show that there was not one bit of legal evidence sufficient to hold any one for trial; as the only thing admitted into the record as evidence, with any semblance of truth, was the defendant's prison record, which the government keeps on record for the purpose of identification,

not for the states to use as evidence and exhibits in a Court of law.

However, your petitioner will not make this copy and contents of the preliminary hearing a part of this writ, but will have it in Court when the writ is heard, to bolster all claims made in reference to it and the evidence used at the trial.

Further, your petitioner will include a certified copy of the additional instructions, that shows a "not guilty" verdict, and two other verdicts brought in by the jury at the said trial, all of which the judge refused to accept, therein sending the jury out to deliberate again without giving them a possibility of bringing back a not guilty verdict.

X.

The following is a certified copy of the "Additional Instructions" given to the jury in the case of the People vs. Cecil E. Humphries, being No. 113274, which is attached hereto and hereby made a part hereof for all purposes with the same force and effect as though herein set forth at length.

Filed Santa Monica, July 7, 1947. A. F. Moroney, County Clerk.

ADDITIONAL JURY INSTRUCTION

Additional Instructions Given in the Case of The
People vs. Cecil E. Humphries, No. 113274.

The Court: The record will show that the defendant and jury are present and that the Deputy

District Attorney has been excused from appearing. Ladies and gentlemen, have you arrived at a verdict?

The Foreman: We have.

The Court: Will you hand the verdict to the bailiff, please? Mr. Pfeiffer, you have signed two forms?

The Foreman: I got the wrong impression. I thought after deciding on the case that we were on, that the other one automatically applied.

The Court: No, that does not necessarily follow. Let the record show that the jury has handed the court three verdict forms, one, not guilty, unsigned, one, guilty of petty theft, a misdemeanor signed by the Foreman, and one a verdict of guilty as charged in the Complaint, and also true, the charge of a prior conviction and service in a penal institution, therefor.

Are the instructions in the list—do you now see what the situation is, Mr. Pfeiffer?

The Foreman: Yes, I believe so.

The Court: Petty theft is an included offense of this charge. The charge is petty theft with a prior conviction of a felony.

The Foreman: Yes, Sir.

The Court: If you find that there was no prior conviction of a felony but that the defendant committed the crime of theft, as otherwise defined in my instructions, then, and in that event only should you bring in a verdict of guilty of petty theft a misdemeanor.

The Foreman: That was our intention.

A Juror: No, it was not.

The Court: Is it your intention to bring in a verdict of petty theft, a misdemeanor, or did you intend to find the defendant guilty as charged in the information?

The Foreman: That is right.

The Court: In order to do that you should take another vote and receive authorization by a unanimous jury, and to return a verdict of guilty of petty theft, a misdemeanor, which is a lesser and included offense, you must find that is the only offense of which the defendant is guilty, if you find he committed the crime of petty theft, and that the prior conviction is not true. Do you follow me?

A Juror: I do not.

The Court: If, however, you believe that you have found that the defendant committed the crime of petty theft and it is true that he was convicted of the felony of burglary in the State of Utah and served a term in the Utah penal institution, then your verdict would be the finding of guilty as charged in the information, and further find the charge of the second conviction and service in a penal institution, therefor, is true. Do you all understand now?

The Foreman: That is what we thought we were doing.

The Court: It is not entirely proper to state what you had intended to arrive at, at this time. Do you now understand what you want to do, in

view of these instructions, when you return to the jury room? Are there any questions of any of you? Shall I go over it again? The defendant is charged with the crime of petty theft and a prior conviction of a felony. If you find him guilty of petty theft and that there was a prior conviction of a felony, and that he served a term in a penal institution, then return a verdict of guilty as charged. If on the other hand, you find him guilty of petty theft as defined in my instructions previously given, but that was not a good prior conviction—that he did not serve a term in a penal institution—then return a verdict of guilty of petty theft. Now what I have said is in no way to detract from the heretofore read instructions. You are not to disregard them in any respect. You are to consider all of them along with these additional instructions which I have now given you, which shall become, and are ordered to become a part of the record in the case. Any other questions now? Reconduct the jury to the jury room, and if and when you have arrived at a verdict announce the same to the bailiff, please, Mr. Pfeiffer.

XII.

(10:00 O'clock p.m.)

The following is office of jury; ruled on by the California Supreme Court, showing that the jury has nothing to do with legal affects, as this case had no facts for the judge to instruct the jury on; as will be seen in the following.

California reports, Tuttle—1874 (No. 4,167).

Office of trial jury. It is the office of a trial jury

by their verdict, to find the facts in issue, whether general or special, and with the legal effect of those facts they have no concern.

XIII.

Dissent of Jury,—Although a jurior may, at the last moment, dissent from a verdict rendered, yet that dissent must be founded on the question of the fact presented by the verdict, and not upon the information received from the verdict of Jury—If jury has special issues submitted to them, and find on these issues, and also find a general verdict for the plaintiff and when the verdict is read, the Court declares that on the findings the defendant must have judgment, and some of the jury then dissent from the special verdict, and the Court sends them out for further deliberation, and they then return with a general verdict, but are unable to agree on the special verdict, the Court should not accept the general verdict.

XIV.

And whereas, pursuant to said judgment and commitment the petitioner's imprisonment has been changed to the Folsom State Prison, in Sacramento County, State of California.

XV.

Wherefore, the said Cecil E. Humphries prays that a writ of Habeas Corpus issue, directed to the said Robert A. Heinze, as Warden of the California State Prison in the United States of America, commanding him the said Robert A. Heinse, as Warden, *supra*, to have and to bring the body of the said Cecil E. Humphries, before and into the

United States District Court, Northern District of California, Sacramento, California, and that the said United States District Court of Northern California, and Hon. Judge Dal M. Lemmon thereof discharge the said Cecil E. Humphries, and order and Secure his Release from such Restraint, and the said Robert A. Heinze, as Warden, do and abide by the Order of the said Court.

Respectfully submitted,

CECIL E. HUMPHRIES,

In pro. per.

State of California,

County of Sacramento—ss.

Cecil E. Humphries, first being duly subscribed and sworn to says and deposes that he is the petitioner for writ of Habeas Corpus, and that he has **read the contents of the foregoing petition** and knows the contents therein to be true to the best of his knowledge; and, also as to those matters related on information and allegations, he believes them to be true.

CECIL E. HUMPHRIES,

In pro. per.

Subscribed and sworn to before me this 14th day of April, 1948.

(Seal)

PETER J. MURRY,

Notary Public in and for the County of Sacramento, State of California.

Notation that filing fee is being paid in full at the same time that the writ is notarized.

[Endorsed): Filed Apr. 21, 1948. C. W. Calbreath, Clerk.

At a stated term of the Northern Division of the United States District Court for the Northern District of California, held at the Court Room thereof, in the City of Sacramento, on Wednesday, the 21st day of April, in the year of our Lord one thousand nine hundred and 48.

Present: The Honorable Dal M. Lemmon, District Judge.

[Title of Cause.]

Due consideration having been had on the application for writ of Habeas Corpus, it is Ordered that the petition for writ of habeas corpus be and the same is hereby denied.

District Court of the United States, Northern
District of California, Northern Division

Notice of Appeal is hereby given that Cecil E. Humphries (being No. 5981) do appeal said action from the above entitled Court within said action was denied on April 21, 1948, to the U. S. Circuit Court of Appeals, whereas, you and each of you are notified here and now to show cause, if you have, why said Appeal should not be granted.

CECIL E. HUMPHRIES.

Sworn to and subscribed before me this 12th day of May, A. D. 1948.

(Seal)

PETER J. MURRY,

Notary Public in and for the County of Sacramento, State of California.

My Commission expires on Sept. 2nd, 1951.

[Endorsed]: Filed May 28, 1948.

CERTIFICATE OF CLERK, U. S. DISTRICT
COURT, TO RECORD ON APPEAL

I, C. W. Calbreath, Clerk of the United States District Court for the Northern District of California, do hereby certify that the foregoing 11 pages, numbered 1 to 11, inclusive, contain a full, true and correct transcript of certain records, and proceedings in the case of Cecil E. Humphries vs. Robert A. Heinze, No. 5981, as the same now remain on file and of record in this office.

I further certify that the cost of preparing and certifying the foregoing Record on Appeal is the sum of Four and 40/100 (\$4.40), and that the same has been paid to me by the appellant herein.

In Witness Whereof, I have hereunto set my hand and the original seal of said District Court, this 12th day of June, A. D. 1948.

(Seal)

C. W. CALBREATH,
Clerk.

/s/ By F. M. Lampert,
Deputy Clerk.

[Endorsed]: No. 11971. United States Circuit Court of Appeals for the Ninth Circuit. Cecil E. Humphries, Appellant, vs. Robert A. Heinze, Warden, etc., Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Northern District of California, Northern Division.

Filed July 13, 1948.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

IN SUPPORT OF PETITION

Office of the Clerk,
U. S. Circuit Court of Appeals,
P.O. Box 547,
San Francisco 1, California,
Mr. Paul P. O'Brien,

Dear Sir:

I am in receipt of a copy of subdivision 6 of Rule 19, which calls for a statement of points on which appellant intends to rely on appeal; as I want the record printed in its entirety; wherein the only and material points needed is the fact that since my conviction, I have been denied without cause of the denial shown, and/or without my appearance in court which was prayed for in the writ. The "question" and only "question", is, has a

judge the power to direct a legal jury to disregard the first "Not Guilty" verdict, and return a second one of a verdict of "Guilty"?

Petitioner contends that the lower courts did not give the writ of error coram nobis or habeas corpus any consideration, which is provided for by the U. S. Constitution; whereas, on a writ of habeas corpus, which in plain English, means "have the body", but petitioner was not present at said court denial; whereas, Article 1, Section 9 of the U. S. Constitution reads:

"The privilege of the writ of habeas corpus shall not be suspended, unless when in cases of rebellion or invasion the public safety may require it."

Please attach the foregoing to said petition, and make it a part thereof, with the same force and effect as though it was original. Here's thanking you in advance, as I remain,

Respectfully,

/s/ CECIL E. HUMPHRIES.

Subscribed and sworn to before me this 23rd day of June, 1948.

(Seal) /s/ LLOYD P. SMITH,

Notary Public in and for the County of Sacramento, State of California.

[Endorsed]: Filed July 13, 1948. Paul P. O'Brien, Clerk.



No. 11972

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

CURTIS COURANT,

Appellant,

vs.

INTERNATIONAL PHOTOGRAPHERS OF THE
MOTION PICTURE INDUSTRY LOCAL 659,
etc., et al.,

Appellees.

TRANSCRIPT OF RECORD

Upon Appeal From the District Court of the United States
for the Southern District of California
Central Division

FILED

SEP 27 1948

PAUL P. O'BRIEN,

CLERK



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Los Angeles 13, Calif. [1*]

In the District Court of the United States for the
Southern District of California
Central Division

Civil Action. File No. 8104 O'C

CURTIS COURANT,

Plaintiff,

vs.

INTERNATIONAL PHOTOGRAPHERS OF THE
MOTION PICTURE INDUSTRY LOCAL 659,
an unincorporated Labor Organization, HERBERT
ALLER, individually and as representative of the
members of said Local 659, DOE 1, DOE 2, DOE 3,
DOE 4, DOE 5, DOE 6, DOE 7, DOE 8, DOE 9,
DOE 10, DOE 11, DOE 12, DOE 13, DOE 14,
DOE 15, DOE 16, DOE 17, DOE 18, DOE 19,
DOE 20, DOE 21, DOE 22, DOE 23, DOE 24,
and DOE 25,

Defendants.

COMPLAINT

Amendment to Complaint ~~Amended:~~

1st date: 5-10-48

I.

Jurisdiction is founded on the existence of a Federal question and the amount in controversy, and on the existence of a question arising under the United States Constitution, Treaty and under particular Federal statutes.

The action arises under the Constitution of the United States, Article 1, Section 8, Article 6, the Fifth Amendment to the Constitution of the United States, the Fourteenth Amendment to the Constitution of the United States; the National Labor Relations Act, 29 U. S. C. A.

151-166, enacted July 5, 1935; Labor Management [2] Relations Act of 1947, 29 U. S. C. A. 141-197, enacted June 23, 1947; the Treaty between the United States and Poland of Friendship, Commerce and Consular Rights, 48 Stat. L. 1507; 28 U. S. C. A. 41 (1, 8, 12, 13, 14, 17, 23); 8 U. S. C. A. 41, 43, under color of Sections 921-923 Labor Code, State of California, and the laws of the State of California, 8 U. S. C. A. 47, 48; 15 U. S. C. A. 15; the matter exceeds, exclusive of interest and costs, the sum or value of \$3,000.00.

II.

The true names or capacities, whether individual, corporate, associate or otherwise, of defendants, Doe 1, Doe 2, Doe 3, Doe 4, Doe 5, Doe 6, Doe 7, Doe 8, Doe 9, Doe 10, Doe 11, Doe 12, Doe 13, Doe 14, Doe 15, Doe 16, Doe 17, Doe 18, Doe 19, Doe 20, Doe 21, Doe 22, Doe 23, Doe 24 and Doe 25, are unknown to plaintiff, who therefore sues said defendants by such fictitious names, and will ask leave to amend this complaint to show their true names and capacities when same have been ascertained.

III.

The International Alliance of Theatrical Stage Employees and Motion Picture Machine Operators of the United States and Canada, hereinafter referred to as IATSE, is a labor organization having as its purpose collective bargaining upon the negotiation of wages, hours and working conditions for its members; officers and agents of the IATSE are engaged in representing and acting for employee members within the above entitled district; IATSE has an office and place of business within said district; the members of the IATSE are members

in good standing of labor organizations having the same purposes and known as local unions and to which the IATSE has issued a charter; there are approximately 1,000 local unions chartered by the IATSE whose members are employed by at least 90% of all employers in the theatrical, television and motion picture industries of the United States; in connection with the motion picture [3] industry members of local unions of the IATSE employed by all employers engaged in the production of motion pictures within the State of California erect the stages for the production of motion pictures, do all work in connection with the filming of scenes of motion pictures, including all labor incidental thereto, as well as doing all make-up work for actors and actresses for motion pictures, and prepare, cut and develop the exposed film for preparation for shipment into intrastate, interstate and foreign commerce; such films are shipped to film exchanges throughout the State of California, the United States and foreign countries and, within the United States and Canada, members of local unions chartered by the IATSE work within said film exchanges; the members of said local unions chartered by the IATSE project the film upon screens in local theatres throughout the State of California, the United States and Canada; all employers engaged in the production of motion pictures within the State of California recognize IATSE as the exclusive bargaining agency for employees engaged in the production of motion pictures as hereinabove defined; the operations of the employers engaged in the production of motion pictures and the operations of the employees engaged in the production of motion pictures, as aforesaid, affect intrastate commerce within the State of California, interstate commerce with the several states of the United States, and foreign commerce; a labor dispute between the

IATSE and employers engaged in the production of motion pictures as aforesaid would completely shut down the production of motion pictures within the State of California and within the United States and would burden and obstruct intrastate, interstate and foreign commerce and the free flow thereof all employees engaged in the production of motion pictures as aforesaid, with the exception of first cameramen (also known as directors of photography) have designated the IATSE as their exclusive bargaining agency on wages, hours and working conditions the IATSE is not and never has [4] been established, maintained or dominated by any employer engaged in the production of motion pictures; ever since January 1, 1943, the IATSE under and by virtue of the National Labor Relations Act and under the color of Sections 921-923 of the Labor Code, State of California, and the laws thereof, has been a party to contracts with all employers engaged in the production of motion pictures, for the benefit of employees engaged in the production of motion pictures as aforesaid, including first cameramen; under said contracts employees engaged in the work as outlined above are required as a condition of employment to maintain membership in the IATSE and its local unions; ever since January 1, 1943, no person employed by any employer engaged in the production of motion pictures as aforesaid wherever manual work was involved has been employed without membership in the IATSE or a work permit from one of its chartered locals.

IV.

Pursuant to the direction of election of the National Labor Relations Board made August 28, 1939, and recorded in Official Records of the Board, 14 N. L. R. B. 224, the National Labor Relations Board did certify the

IATSE and its various local unions composed of members engaged in the production of motion pictures as aforesaid as the exclusive bargaining agency for all of said employees, with the exception of first cameramen; that the Official Record of said certification is found in 15 N. L. R. B. 225; said certification is still in force and effect; the IATSE represents some 10,000 employees engaged in the production of motion pictures within the State of California, County of Los Angeles.

V.

A first cameraman is a highly skilled person with many years of experience in all phases of motion picture camera work who is responsible for the artistic photographic effect of the action of the camera upon scenes taken for motion pictures, including the lighting thereof, the camera angles and the like, and is solely [5] responsible for the photographic results on the screen.

VI.

The American Society of Cinemaphotographers, hereinafter referred to as ASC, was from prior to 1941, and until the end of 1942, a labor organization composed of first cameramen for the purpose of collective bargaining on the part of all first cameramen upon wages, hours and working conditions of first cameramen with employers engaged in the production of motion pictures within the State of California; during said period the ASC represented a majority of first cameramen in said State and there was in force and effect contracts with all employers within said State requiring that as a condition of employment first cameramen be members of the ASC; the ASC was not established, maintained or dominated by any employer; no person could be employed by any em-

ployer engaged in the production of motion pictures within said State unless he were a member of ASC; on or about December 10, 1942, all members of the ASC designated the defendant, International Photographers of the Motion Picture Industry, Local 659, an unincorporated labor organization, hereinafter referred to as Local 659, as their collective bargaining agent to represent them on wages, hours and working conditions.

VII.

Local 659 is a labor organization having as one of its purposes the collective bargaining with employers upon negotiation of wages, hours and working conditions for its members; that officers and agents of Local 659 are engaged in representing and act for employee members within the above entitled district, and Local 659 maintains its principal office therein; on December 10, 1942, and all times thereafter Local 659 was a chartered local union of the IATSE; ever since December 10, 1942, Local 659 has been designated by a majority of first cameramen in said State of California as their exclusive bargaining agency on [6] wages, hours and working conditions and, ever since the said date, Local 659 has represented first cameramen in negotiations with all employers engaged in the production of motion pictures within said State as aforesaid; that Local 659 is not established, maintained or dominated by any employer; ever since December 10, 1942, there has been no controversy between any employer and Local 659 as to whether or not Local 659 was the exclusive bargaining agency for first cameramen on wages, hours and working conditions of first cameramen; at all times since that date Local 659 has acted as the exclusive bargaining agency on wages, hours and working conditions of first cameramen; pursuant to, by virtue of

and under the color of the authority granted to it by the National Labor Relations Act, Sections 921-923 of the Labor Code of the State of California, and the law of the State of California, Local 659, on or about January 1, 1943, entered into contracts with all employers engaged in the production of motion pictures as aforesaid within the State of California, requiring as a condition of employment that all first cameramen be and remain members in good standing of Local 659, a contract with such provision being commonly known as a closed shop contract; closed shop contracts for first cameramen between Local 659 and all employers engaged in the motion picture industry within said State have remained in full force and effect from on or about January 1, 1943, to and including the date of the filing of this complaint; the last agreement entered into by and between IATSE, Local 659, and all employers engaged in the production of motion pictures in said State was executed in writing as of January 1, 1946, for a term ending December 31, 1948, and provides that Local 659 shall represent all first cameramen for the purpose of collective bargaining and that employers engaged in the production of motion pictures will employ only first cameramen who are members in good standing of Local 659, and that Local 659 will furnish competent men to perform the work and render the services required by the [7] employer of first cameramen; a labor dispute between Local 659 and employers engaged in the production of motion pictures as aforesaid concerning first cameramen would completely shut down the production of motion pictures within the State of California and would burden and obstruct intrastate commerce, interstate commerce and foreign commerce and the free flow thereof.

VIII.

The State of California is the center within the United States of the production of motion pictures and the majority in the amount of exposed film and value of products in the production of motion pictures within the United States are produced within said State; the majority of employees engaged in the production of motion pictures as hereinabove set forth are employed for each individual picture produced or a lesser period; many first cameramen, members of Local 659 and beneficiaries under said closed shop contracts, are employed for each picture produced or for a lesser period.

IX.

Plaintiff was born on May 11, 1899, in Katowice, then under the sovereignty of the German Empire; during the year 1921, Katowice became under the sovereignty of Poland; plaintiff entered the United States with a United States immigration visa under Polish quota on or about the 28th day of May, 1941, at the Port of New York, all in accordance with Federal statutes as provided therefor; plaintiff did on or about the 10th day of July, 1941, file with the United States of America his declaration of intention to become a citizen of the United States; on the 11th day of July, 1947, plaintiff became a citizen of the United States of America and thereafter received his Certificate of Naturalization from the Clerk of the above entitled court; ever since the 1st day of July, 1941, plaintiff has intended to make his home within the State of California, and ever since said date has been a resident of the State of California, and intends to make his home in said State [8] permanently; beginning in 1920, plaintiff commenced his training and experience for first cameraman and learned all phases of the art or craft of

first cameraman; thereafter and until the outbreak of World War II, plaintiff acted as first cameraman in France, England, Italy, German, Austria and Hungary, and for the period up until he entered the United States was the first cameraman for in excess of 200 pictures produced in said countries; many of said pictures were shown and favorably received in local theaters in the United States, including "Quo Vadis," starring Emil Jannings, "Louise," starring Grace Moore, "The Human Beast," starring Jean Gabin, and "Broken Blossoms," starring Dolly Haas; upon entry into the United States in 1941, and ever since, plaintiff has had a high reputation within the United States and the State of California as a first cameraman; the said reputation of plaintiff was known among the employers, directors, actors and actresses of the motion picture industry within the State of California.

X.

For the period commencing with plaintiff's entry into the United States in 1941, to and including the end of December, 1942, plaintiff applied for membership in ASC and did all things requested in connection with filing his application with ASC; that ASC refused to admit plaintiff to membership in said union; as a result thereof plaintiff was unable to work as first cameraman during the period to the end of 1942.

XI.

Continuously ever since January, 1942, plaintiff has been filing his application for membership in the manner required by Local 659 on the forms supplied by Local 659, has deposited with Local 659 the sum of \$250.00, being one-half the initiation fee for membership in

Local 659 and has obtained the signatures of three members of Local 659, all as required by Local 659, and has done all things required by Local 659 of an applicant for membership; that [9] ever since January 1, 1942, Local 659 has refused to admit plaintiff to membership therein and, with the exceptions hereinafter noted, has refused to permit plaintiff to work as a first cameraman for any employer engaged in the production of motion pictures within the State of California.

XII.

Local 659 is composed of several hundred members and it is impractical to join all of said members as defendants in the above entitled action; defendant Herbert Aller is the Business Representative of all the members of Local 659 and acts for and on behalf of all members of Local 659, in connection with all their activities as described herein, and is sued herein individually and in his representative capacity of all members of Local 659; the members of Local 659 and Herbert Aller have entered into a conspiracy to deprive plaintiff of working as a first cameraman within the State of California, and have threatened great and irreparable damage to any employer who would employ plaintiff as a first cameraman within said State; that the acts constituting the conspiracy referred to are as set forth in this complaint.

XIII.

Ever since January 1, 1943, Local 659 has not admitted to membership any first cameraman although qualified persons have applied for membership and complied with all rules and regulations relating to applicants to membership in Local 659.

XIV.

Defendants and members of Local 659, ever since January 1, 1942, have conspired together by the means of the closed shop contracts above referred to and by means of refusing to admit any first cameraman to membership in said union, and by means of the other acts as set forth in this complaint, to monopolize for themselves all positions of first cameramen within the motion picture industry in the State of California; such acts are in violation of the [10] Constitution of California, Article I, and are an unlawful restraint on commerce and trade within the State of California and upon interstate and foreign commerce.

XV.

The defendants and the members of Local 659 have, ever since January 1, 1942, known that plaintiff was a qualified first cameraman, and that he entered the United States on a United States immigration visa, and that he filed his declaration of intention to become a citizen of the United States on or about July 10, 1941, and that since July 11, 1947, he was a citizen of the United States, and have known that plaintiff was dependent for his livelihood on work as a first cameraman and have known that plaintiff was suffering great humiliation and worry as a result of their continued refusal to permit plaintiff to membership in Local 659; defendants and members of Local 659, from January 1, 1942, and continuously up to the date of the filing of this complaint, have refused to admit plaintiff to membership in said Local 659; each time the application of plaintiff came before the membership for consideration, the only question discussed was whether plaintiff might obtain work as first cameraman, and the membership, believing that he would, therefore

denied his application; it is useless for plaintiff to file any further applications for or to do any other act required of applicants of Local 659.

XVI.

Ever since January 1, 1942, the Constitution of the IATSE, Article I, Section 3 thereof, has provided that "No person shall be eligible to membership in said Alliance who is not a citizen of the United States or Canada, or of any other territory in which the Alliance exercises jurisdiction;" the defendants and members of Local 659 consider said provision to be binding on each of them and have, ever since January 1, 1942, until July 11, 1947, as one of the grounds of refusal refused to admit plaintiff to membership in the [11] IATSE and Local 659 under and by virtue of said provision of their Constitution.

XVII.

The By-Laws of Local 659 and the members thereof for more than a year last past have provided that no first cameraman shall be admitted to said union.

XVIII.

Ever since January 1, 1942, defendants and members of Local 659 have refused to admit plaintiff as a member and in connection therewith have never advised plaintiff of any reason for denial of membership except that such membership was contrary to their Constitution or that employment as first cameraman was desired for the members of Local 659.

XIX.

Continuously, ever since plaintiff entered the United States, plaintiff has received offers of employment as first cameraman from employers engaged in the production of

motion pictures as aforesaid within the State of California on the condition that plaintiff for the period ending 1942, be a member of ASC, and thereafter on the condition that plaintiff be a member of Local 659; that plaintiff has been unable to accept said offers because he was not a member of said unions, with the exception that defendants permitted plaintiff to be employed by employers on three productions of motion pictures, one in 1945, entitled "Mad Wednesday," produced by California Pictures Corporation, another in 1946, entitled "Monsieur Verdoux," produced by Charlie Chaplin Studios, and another in 1947, entitled "Song of My Heart," produced by Allied Artists Corporation, under the terms and conditions as laid down by the defendants; said terms and conditions were as follows: Plaintiff could not look into the camera, nor touch the camera, nor give any order or direction to any of the camera crew, and plaintiff's employer was required to employ an extra union first cameraman; that plaintiff carefully [12] carried out all of these demands and conditions of defendants and plaintiff did have responsibility in connection with these three motion pictures produced in the State of California for the artistic effect on the screen, acting via the director of the motion picture through the extra union first cameraman, during 1946, Warner Bros. Pictures, Inc. offered employment to plaintiff on the motion picture "Possessed," starring Joan Crawford, under the same terms and conditions as laid down by defendants, but defendants refused to permit Warner Bros. Pictures, Inc. to so employ plaintiff; with the exception of the three employments referred to it has been and will be impossible for plaintiff to obtain similar employment under said terms and conditions as laid down by the defendants; that for said work on said three motion pictures as an employee

of the producers of motion pictures within the State of California plaintiff was paid approximately \$19,000.00 for a period of approximately eight months' work; plaintiff during the time of World War II was requested to act as first cameraman for a period of approximately five months for the War Department of the United States Government and was paid a sum of approximately \$800.00 therefor.

XX.

But for the action of the defendants as set forth in this complaint for the period beginning January 1, 1943, to the date of the filing of this complaint, plaintiff would have earned the sum of \$125,000.00, excluding therefrom the amounts plaintiff earned as hereinabove set forth, and the plaintiff has been damaged by the acts of the defendants and members of Local 659 in the amount of \$125,000.00.

XXI.

The defendants and members of Local 659 threaten to and will continue to prevent plaintiff from becoming a member of the union and will prevent him from following his occupation of first cameraman within the State of California for the remainder of [13] plaintiff's active life as a first cameraman, to the damage of plaintiff in the sum of \$250,000.00.

XXII.

That plaintiff has suffered great humiliation, worry, frustration and loss of prestige from the acts of the defendants complained of, to his damage in the sum of \$100,000.00.

XXIII.

The defendants for many years past and ever since January 1, 1942, have been warned that their refusal to admit persons to membership under the conditions outlined herein was in violation of law, but, nevertheless, the defendants have sought to deprive plaintiff of his rights under the Constitution of the United States, Treaties and Statutes of the United States for the selfish purpose of maintaining all the jobs of first cameraman for the members of Local 659, and that the aforesaid actions of the defendants are wanton, wilful and malicious and that exemplary damages should be imposed on defendants in the sum of \$500,000.00.

Wherefore, plaintiff prays for judgment against the defendants:

1. For loss of earnings in the sum of \$125,000.00, and that the same be trebled;
2. For loss of future employment in the sum of \$250,000.00, and that the same be trebled;
3. For general damages in the sum of \$100,000.00, and that the same be trebled;
4. For exemplary damages in the sum of \$500,000.00; and
5. For reasonable attorney's fees, costs of suit incurred and for such other relief as may be meet and just in the premises.

HENRY B. ELY

Attorney for Plaintiff

[Endorsed]: Filed Apr. 6, 1948. Edmund L. Smith,
Clerk. [14]

[Title of District Court and Cause]

MOTIONS BY DEFENDANTS INTERNATIONAL PHOTOGRAPHERS OF THE MOTION PICTURE INDUSTRY LOCAL 659, AN UNINCORPORATED LABOR ORGANIZATION, HEREINAFTER REFERRED TO AS DEFENDANT LOCAL, AND HERBERT ALLER, INDIVIDUALLY AND AS REPRESENTATIVE OF THE MEMBERS OF SAID LOCAL 659, HEREINAFTER REFERRED TO AS DEFENDANT ALLER, TO DISMISS

The Defendant Local and Defendant Aller, and Each of Them, Severally Move the Court as Follows:

(1) To dismiss the action on the ground that the Court lacks jurisdiction over the subject matter for the reason that jurisdiction is not vested in this Court by the Constitution of the United States, Article 1, Section 8, Article 6, the Fifth Amendment to the Constitution of the United States, the Fourteenth [15] Amendment to the Constitution of the United States; the National Labor Relations Act, 29 U. S. C. A. 151-166, enacted July 5, 1935; Labor Management Relations Act of 1947, 29 U. S. C. A. 141-197, enacted June 23, 1947; the Treaty between the United States and Poland of Friendship, Commerce and Consular Rights, 48 Stat. L. 1507; 28 U. S. C. A. 41 (1, 8, 12, 13, 14, 17, 23); 8 U. S. C. A. 41, 43, under color of Sections 921-923 Labor Code, State of California, and the laws of the State of California, 8 U. S. C. A. 47, 48; 15 U. S. C. A. 15); nor by any provision of the Constitution of the United States; nor by any provision of the Statutes or Laws of the United States; nor by any provision of any treaty to which the United States is a party.

(2) To dismiss the action on the ground that the Court lacks jurisdiction because, as appears from the face of the Complaint, the diversity of citizenship necessary for jurisdiction does not exist.

(3) To dismiss the action as to the Defendant Local because the Complaint fails to state a claim against said defendant upon which relief can be granted.

(4) To dismiss the action as to Defendant Aller because the Complaint fails to state a claim against said defendant upon which relief can be granted.

(5) To dismiss the action because the Complaint fails to state a claim against the Defendant Local or Defendant Aller, jointly or severally, upon which relief can be granted.

This motion will be made upon the Complaint on file herein, the Notice of Motion and Points and Authorities in support thereof, and the Affidavit of Defendant Aller, hereto attached, by reference incorporated herein and made a part hereof. [16]

Dated: April 26, 1948.

BODKIN, BRESLIN & LUDDY
HENRY G. BODKIN
GEORGE M. BRESLIN
MICHAEL G. LUDDY

By Michael G. Luddy

453 South Spring Street
Los Angeles 13, California
Phone: MUtual 3151

Attorneys for Defendants International Photographers of the Motion Picture Industry Local 659, an Unincorporated Labor Organization, and Herbert Aller, Individually and as Representative of the Members of Said Local 659

NOTICE OF MOTION

To: Henry B. Ely, Esq.
453 South Spring Street
Los Angeles 13, California
Attorney for Plaintiff

Please Take Notice that the undersigned will bring the above motions on for hearing before this Court at the Court Room of the Honorable J. F. T. O'Connor, Court Room No. 7 of the United States Post Office and Court House Building, in the City of Los Angeles, County of Los Angeles, State of California, on Monday, the 10th day of May, 1948, at 10:00 o'clock in the forenoon of that day, or as soon thereafter as counsel may be heard.

Dated: April 26, 1948.

BODKIN, BRESLIN & LUDDY
HENRY G. BODKIN
GEORGE M. BRESLIN
MICHAEL G. LUDDY

By Michael G. Luddy

453 South Spring Street
Los Angeles 13, California
Phone: MUtual 3151

Attorneys for Above Named Defendants [17]

Received copy of the within Motions, etc., to Dismiss and Notice thereof this 26th day of April, 1948. Henry B. Ely, Attorney for Plaintiff.

[Endorsed]: Filed Apr. 26, 1948. Edmund L. Smith, Clerk. [18]

[Title of District Court and Cause]

MOTION BY DEFENDANT THE INTERNATIONAL ALLIANCE OF THEATRICAL STAGE EMPLOYEES AND MOTION PICTURE MACHINE OPERATORS OF THE UNITED STATES AND CANADA (SUED HEREIN AS DOE 1), HEREINAFTER REFERRED TO AS THE ALLIANCE, TO DISMISS

Defendant The Alliance Moves the Court as Follows:

(1) To dismiss the action on the ground that the Court lacks jurisdiction over the subject matter for the reason that jurisdiction is not vested in this Court by the Constitution of the United States, Article 1, Section 8, Article 6, the Fifth Amendment to the Constitution of the United States, the Fourteenth Amendment to the Constitution of the United States; the National Labor Relations Act, 29 U. S. C. A. 151-166, enacted July 5, 1935; [19] Labor Management Relations Act of 1947, 29 U. S. C. A. 141-197, enacted June 23, 1947; the Treaty between the United States and Poland of Friendship, Commerce and Consular Rights, 48 Stat. L. 1507; 28 U. S. C. A. 41 (1, 8, 12, 13, 14, 17, 23); 8 U. S. C. A. 41, 43, under color of Sections 921-923 Labor Code, State of California, and the laws of the State of California, 8 U. S. C. A. 47, 48; 15 U. S. C. A. 15); nor by any provision of the Constitution of the United States; nor by any provision of the Statutes or Laws of the United States; nor by any provision of any treaty to which the United States is a party.

(2) To dismiss the action on the ground that the Court lacks jurisdiction because, as appears from the face of the Complaint, the diversity of citizenship necessary for jurisdiction does not exist.

(3) To dismiss the action because the Complaint fails to state a claim against said defendant upon which relief can be granted.

This motion will be made upon the Complaint on file herein, the Notice of Motion and Points and Authorities in support thereof, and the Affidavit of Roy M. Brewer, hereto attached, by reference incorporated herein and made a part hereof.

Dated: April 28, 1948.

BODKIN, BRESLIN & LUDDY
HENRY G. BODKIN
GEORGE M. BRESLIN
MICHAEL G. LUDDY

By Michael G. Luddy

453 South Spring Street
Los Angeles 13, California
Phone: MUtual 3151

Attorneys for Defendant The Alliance [20]

NOTICE OF MOTION

To: Henry B. Ely, Esq.
453 South Spring Street
Los Angeles 13, California
Attorney for Plaintiff

Please Take Notice that the undersigned will bring the above motion on for hearing before this Court at the Court Room of the Honorable J. F. T. O'Connor, Court Room No. 7 of the United States Post Office and Court House Building, in the City of Los Angeles, County of Los Angeles, State of California, on Monday, the 10th day of May, 1948, at 10:00 o'clock in the forenoon of that day, or as soon thereafter as counsel may be heard.

Dated: April 28, 1948.

BODKIN, BRESLIN & LUDDY
HENRY G. BODKIN
GEORGE M. BRESLIN
MICHAEL G. LUDDY

By Michael G. Luddy

453 South Spring Street
Los Angeles 13, California
Phone: MUtual 3151

Attorneys for Defendant The Alliance [21]

Received copy of the within Motion, etc., to Dismiss and Notice thereof this 28th day of April, 1948. Henry B. Ely, Attorney for Plaintiff.

[Endorsed]: Filed Apr. 28, 1948. Edmund L. Smith, Clerk. [22]

[Title of District Court and Cause]

AMENDMENT TO COMPLAINT

Plaintiff amends his complaint on file herein as follows:

I.

By adding to paragraph I of the complaint:

“the Preamble and Articles 1, 2, 55 and 56 of the United Nations Charter (59 Stat. L. 1046).”

II.

By adding to paragraph XVI, at the end thereof, the following:

“Such provision of the Constitution of the IATSE is unreasonable, arbitrary, capricious and without justification.”

III.

By adding to paragraph XVII, at the end thereof, the following: [23]

“That such provisions of the By-Laws of Local 659 are unreasonable, arbitrary, capricious and without justification.”

HENRY B. ELY

Attorney for Plaintiff

[Endorsed]: Filed May 10, 1948. Edmund L. Smith, Clerk. [24]

[Title of District Court and Cause]

OPINION

Henry B. Ely, Los Angeles, California,
representing the plaintiff.

Bodkin, Breslin & Luddy, Los Angeles,
California, representing the defendants.

O'Connor, J. F. T., Judge.

This is an action by the plaintiff, Curtis Courant, against International Photographers of the Motion Picture Industry Local 659, an unincorporated labor organization, et al. The complaint was filed on April 6, 1948 and amendment filed May 10, 1948.

In his statement of the case, the plaintiff stated the
in his brief [O'Connor, Judge]
controversy [^] as follows:

"Plaintiff as an alien with Declaration of Intention on file, and as a citizen, filed his complaint for damages in the above action on the ground that defendants both refused to permit him to work because of their closed shop agreement, and refused to admit him to membership in their unions." There seems to be a contradiction in the statement: plaintiff could not be both an alien with declaration on file, and a citizen. However, the allegation in the complaint is controlling, which states as follows: [25]

" . . . on the 11th day of July, 1947, plaintiff became a citizen of the United States of America and thereafter received his certificate of naturalization from the clerk of the above entitled court; ever since the first day of

July, 1941, plaintiff has intended to make his home within the State of California and ever since said date has been a resident of the State of California and intends to make his home in said state permanently”

The plaintiff alleges he complied with all of the rules and regulations of Local 659 in filing his application for membership, and deposited with Local 659 the sum of \$250.00, being one-half of the initiation fee for membership, and, further, obtained the signature of three members of Local 659, and has done all things required of an applicant for membership. Notwithstanding this compliance, he has been denied membership.

Plaintiff further alleges:

“Defendants and members of Local 659, ever since January 1, 1942, have conspired together by the means of the closed shop contracts above referred to and by means of refusing to admit any first cameraman to membership in said union, and by means of the other acts as set forth in this complaint, to monopolize for themselves all positions of first cameramen within the motion picture industry in the State of California; such acts are in violation of the Constitution of California, Article I, and are an unlawful restraint on commerce and trade within the State of California and upon interstate and foreign commerce.”

On April 26, 1948 the defendants filed a motion to dismiss the complaint on the following grounds—

“(1) To dismiss the action on the ground that the Court lacks jurisdiction over the subject matter for the

[26] reason that jurisdiction is not vested in this Court by the Constitution of the United States, Article 1, Section 8, Article 6, the Fifth Amendment to the Constitution of the United States, the Fourteenth Amendment to the Constitution of the United States; the National Labor Relations Act, 29 U. S. C. A. 151-166, enacted July 5, 1935; Labor Management Relations Act of 1947, 29 U. S. C. A. 141-197, enacted June 23, 1947; the Treaty between the United States and Poland of Friendship, Commerce and Consular Rights, 48 Stat. L. 1507; 28 U. S. C. A. 41 (1, 8, 12, 13, 14, 17, 23); 8 U. S. C. A. 41, 43, under color of Sections 921-923 Labor Code, State of California, and the laws of the State of California, 8 U. S. C. A. 47, 48; 15 U. S. C. A. 15); nor by any provision of the Constitution of the United States; nor by any provision of the Statutes or Laws of the United States; nor by any provision of any treaty to which the United States is a party.

“(2) To dismiss the action on the ground that the Court lacks jurisdiction because, as appears from the face of the Complaint, the diversity of citizenship necessary for jurisdiction does not exist.

“(3) To dismiss the action as to the Defendant Local because the Complaint fails to state a claim against said defendant upon which relief can be granted.

“(4) To dismiss the action as to Defendant Aller because the Complaint fails to state a claim against said defendant upon which relief can be granted.

“(5) To dismiss the action because the Complaint fails to state a claim against the Defendant Local or Defendant Aller, jointly or severally, upon which relief can be granted. [27]

“This motion will be made upon the Complaint on file herein, the Notice of Motion and Points and Authorities in support thereof, and the Affidavit of Defendant Aller, hereto attached, by reference incorporated herein and made a part hereof.”

A similar action was filed in this court and decided by Judge Ben Harrison:

Schatte, et al. v. International Alliance, etc., et al.,
70 Fed. Supp. 1008; Affirmed: 165 Fed. (2d)
216. (Petition for Writ of Certiorari denied by
the Supreme Court of the United States.) (8
U. S. Sup. Ct. Bulletin No. 23, p. 1327; 16 Law
Week 3316 and 3332.)

The motion of defendants to dismiss is granted.

Exception allowed the plaintiff.

Dated at Los Angeles, California, this 27th day of May,
1948.

J. F. T. O'CONNOR

United States District Judge

[Endorsed]: Filed May 27, 1948. Edmund L. Smith,
Clerk. [28]

In the District Court of the United States for the
Southern District of California
Central Division

No. 8104, O'C

CURTIS COURANT,

Plaintiff,

vs.

INTERNATIONAL PHOTOGRAPHERS OF THE
MOTION PICTURE INDUSTRY LOCAL 659,
an unincorporated Labor Organization, et al.,
Defendants.

JUDGMENT OF DISMISSAL FOR LACK OF JURISDICTION

The motions of the defendants International Photographers of the Motion Picture Industry Local 659, an unincorporated labor organization, The International Alliance of Theatrical Stage Employees and Motion Picture Machine Operators of the United States and Canada, an unincorporated labor organization, and Herbert Aller, individually, and as representative of the members of said Local 659, for the dismissal of the above entitled action for lack of jurisdiction of this Court, having heretofore been submitted to this Court for determination, and it appearing that this Court lacks jurisdiction to proceed in said action: [29]

It is therefore ordered, adjudged and decreed that the above entitled action be and is hereby dismissed for lack of jurisdiction.

Dated: This 1st day of June, 1948.

J. F. T. O'CONNOR

Judge

Approved as to form. Henry B. Ely, Attorney for Plaintiff. Dated: This 27th day of May, 1948.

Judgment entered Jun. 1, 1948. Docketed Jun 1, 1948. Book C. O. B. 51, page 100. Edmund L. Smith, Clerk; By Francis E. Cross, Deputy.

[Endorsed]: Filed Jun. 1, 1948. Edmund L. Smith, Clerk. [30]

[Title of District Court and Cause]

NOTICE OF APPEAL TO CIRCUIT COURT OF
APPEALS UNDER RULE 73(b)

Notice Is Hereby Given that Curtis Courant, plaintiff above-named, hereby appeals to the Circuit Court of Appeals for the Ninth Circuit from the Final Judgment of Dismissal for Lack of Jurisdiction entered in this action on the 1st day of June, 1948.

Dated this 4th day of June, 1948.

HENRY B. ELY

Attorney for Plaintiff and Appellant,

CURTIS COURANT

[Endorsed]: Filed & mld. copy to Bodkin, Breslin & Luddy, Attys. for Defts. Jun. 3, 1948. Edmund L. Smith, Clerk. [31]

[Title of District Court and Cause]

STATEMENT OF POINTS OF PLAINTIFF AND
APPELLANT UNDER RULE 75(d)

The plaintiff and appellant will rely on the following points on appeal to sustain jurisdiction of the District Court:

1. The District Court has jurisdiction of the action under the National Labor Relations Act, 29 U. S. C. A. 151-166; Fifth Amendment to the Constitution, and Article 1, Section 8 and Article 6 thereof; the United States Treaty with Poland, 48 Stat. L. 1507; 28 U. S. C. A. 41 (1, 8, 12, 13, 14, 17, 23); 8 U. S. C. A. 47-48; 15 U. S. C. A. 15; United Nations Charter, the Preamble and Articles 1, 2, 55 and 56 thereof (59 Stat. L. 1046); 8 U. S. C. A. 41, 43, under color of Sections 921-923 Labor Code, State of California.

2. Appellant claims rights under the National Labor Relations Act, the Constitution, Treaties and Laws of the United States; the District Court has jurisdiction to determine whether or not appellant has any rights under such laws. [32]

3. The Congress under the National Labor Relations Act, has clothed appellees with monopolistic legislative powers and under the Act and the common law applicable thereto, appellees have violated their duty toward appellant, a Federal question.

4. Appellant is an employee as defined by the National Labor Relations Act; has been employed as First Camera-

man, has had offers of employment and appellees are estopped from claiming appellant not to be an employee; appellees have denied to appellant his rights as guaranteed under Section 7 of the National Labor Relations Act.

5. If, under Congressional authority, appellees have the right to prevent appellant from entering into a contract of hire, then questions of constitutionality of the National Labor Relations Act arise, a Federal question, and a conflict arises between the California Constitution and the National Labor Relations Act.

6. The portions of the Treaty with Poland relied on by appellant are self-executing, binding on the appellees as congressionally clothed agencies, and in their private capacities, and protect appellant in his accepting an offer of hire, a Federal question.

7. The monopoly of the appellees is forbidden by the Anti-Trust Laws, a Federal question.

Dated: June 4, 1948.

HENRY B. ELY

Attorney for Plaintiff and Appellant [33]

Received copy of the within this 4th day of June, 1948.
Michael G. Luddy, Attorney for Defendants.

[Endorsed]: Filed Jun. 4, 1948. Edmund L. Smith,
Clerk. [34]

[Title of District Court and Cause]

CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the District Court of the United States for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 36, inclusive, contain full, true and correct copies of Complaint; Motions of Defendants International Photographers of the Motion Picture Industry Local 659 et al. and International Alliance of Theatrical Stage Employees and Motion Picture Machine Operators of the United States and Canada to Dismiss; Amendment to Complaint; Opinion; Judgment of Dismissal for Lack of Jurisdiction; Notice of Appeal; Statement of Points under Rule 75(d); and Stipulation as to Record under Rule 75(f) which constitute the record on appeal to the United States Circuit Court of Appeals for the Ninth Circuit.

I further certify that my fees for preparing, comparing, correcting and certifying the foregoing record amount to \$9.70 which sum has been paid to me by appellant.

Witness my hand and the seal of said District Court this 13 day of July, A. D. 1948.

(Seal)

EDMUND L. SMITH
Clerk

By Theodore Hocke
Chief Deputy

[Endorsed]: No. 11972. United States Circuit Court of Appeals for the Ninth Circuit. Curtis Courant, Appellant, vs. International Photographers of the Motion Picture Industry Local 659, etc., et al., Appellees. Transcript of Record. Upon Appeal From the District Court of the United States for the Southern District of California, Central Division.

Filed July 14, 1948.

PAUL P. O'BRIEN

Clerk of the United States Circuit Court of Appeals for
the Ninth Circuit



No. 11972

IN THE

United States Court of Appeals
FOR THE NINTH CIRCUIT

CURTIS COURANT,

Appellant,

vs.

INTERNATIONAL PHOTOGRAPHERS OF THE MOTION PIC-
TURE INDUSTRY LOCAL 659, ETC., *et al.*,

Appellees.

OPENING BRIEF OF APPELLANT.

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No. 11972

IN THE

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FOR THE NINTH CIRCUIT

CURTIS COURANT,

Appellant,

vs.

INTERNATIONAL PHOTOGRAPHERS OF THE MOTION PICTURE
INDUSTRY LOCAL 659, ETC., *et al.*,

Appellees.

OPENING BRIEF OF APPELLANT.

Preliminary Statement.

The appellant filed a civil action for damages in the Federal District Court against the appellee unions and their representatives. The appellant alleged that he came to this country in 1941, with twenty years' experience as a first cameraman in the motion picture business. The complaint states that from the date of his arrival to the time of the filing of the complaint, April 6, 1948, the first cameramen in the industry, acting through their exclusive bargaining representatives under the National Labor Relations Act, prevented appellant from working because of non-membership in their unions, and at the same time refused to admit him to membership. Appellant further alleged that from 1941 until 1947 the unions would not act favorably upon his applications for membership because

he was not a citizen; from 1947, when he became a citizen, until the filing of this action, the unions turned down his applications, saying that no more first cameramen would be admitted to the unions. Ever since January, 1943, while the appellee unions acted as exclusive bargaining representatives, they refused to permit appellant to work (except on three occasions) although appellant had continuous offers of employment. The appellant alleged that the motion picture industry, in which he had been offered employment, affected interstate commerce within the meaning of the National Labor Relations Act [Tr. 2-16, 23]. The claim of appellant is founded on his right, under Section 7 of the National Labor Relations Act, to join labor organizations and on the duties of appellee unions to appellant, as the exclusive bargaining representatives of all cameramen under Section 9 of the same act.

The appellee unions filed motions to dismiss for lack of jurisdiction [Tr. 17-21] and after Opinion [Tr. 24-27] the District Court rendered its Judgment of Dismissal for lack of jurisdiction [Tr. 28-29].

The sole question presented by the appeal in this case is whether or not a Federal Court should determine the rights, if any, of the appellant under the Constitution of the United States, the National Labor Relations Act, the Polish Treaty, and the other statutes hereinafter referred to. In other words, has the appellant, under his pleadings, raised a substantial question as to whether or not he has any protection under Federal law which would require the Federal District Court to decide either for or against him, under the provisions of the Federal Constitution and statutes upon which he relies. This Court need not decide what those rights are, but merely direct the District Court to adjudicate the questions.

We quote from Paragraph I of appellant's complaint as amended, which sets forth the grounds of Federal jurisdiction:

"Jurisdiction is founded on the existence of a Federal question and the amount in controversy, and on the existence of a question arising under the United States Constitution, Treaty and under particular Federal statutes.

"The action arises under the Constitution of the United States, Article 1, Section 8, Article 6, the Fifth Amendment to the Constitution of the United States, the Fourteenth Amendment to the Constitution of the United States; the National Labor Relations Act, 29 U. S. C. A. 151-166, enacted July 5, 1935; Labor Management [2] Relations Act of 1947, 29 U. S. C. A. 141-197, enacted June 23, 1947; the Treaty between the United States and Poland of Friendship, Commerce and Consular Rights, 48 Stat. L. 1507; 28 U. S. C. A. 41 (1, 8, 12, 13, 14, 17, 23); 8 U. S. C. A. 41, 43, under color of Sections 921-923 Labor Code, State of California, and the laws of the State of California, 8 U. S. C. A. 47, 48; 15 U. S. C. A. 15; the matter exceeds, exclusive of interest and costs, the sum or value of \$3,000.00; the Preamble and Articles 1, 2, 55 and 56 of the United Nations Charter (59 Stat. L. 1046)." [Tr. 2-3, 23.]*

*Effective September 1, 1948, Title 28 of United States Code was revised and the sections of that title above referred to are renumbered as follows:

Title 28, 41 (Old)	Title 28 (New)
1	1331
8	1337
12	1343
13	1343
14	1343
17	1350
23	1337

The express provisions of the Federal law relied upon are set forth in the Appendix as follows:

- | | |
|---|------------------------|
| Constitution of the United States, Article I, Section 8; Article VI; Fifth Amendment; Fourteenth Amendment. | Appendix "A," page 1. |
| National Labor Relations Act of 1935, Sections 1, 2, 7, 8 and 9. | Appendix "B," page 2. |
| Treaty between the United States and Poland of Friendship, Commerce and Consular Rights, 48 Stat. L. 1507. | Appendix "C," page 4. |
| United Nations Charter, Preamble, Articles 1, 2, 55 and 56 (59 Stat. L. 1046). | Appendix "D," page 8. |
| 28 U. S. C. A. 41 (1, 8, 12, 13, 14, 17, 23) and 28 U. S. C. 1331, 1337, 1343 and 1350. | Appendix "E," page 12. |
| 8 U. S. C. A. 41, 43, 47. | Appendix "F," page 15. |
| Labor Code, State of California, Sections 921-923. | Appendix "G," page 16. |
| Labor Management Relations Act, 1947, Section 301(c). | Appendix "H," page 18. |
| 15 U. S. C. A. 15. | Appendix "I," page 18. |

Statement of the Case.

We are not concerned in this case with the relative rights and duties of unions as they may have existed prior to the National Labor Relations Act of 1935. Until 1935, so far as the Federal Government was concerned, labor unions were left relatively free to gain what strength they might in a "dog eat dog" fight with employers. The employer had the advantage of discharging a union employee as soon as he wore his union badge, refusing to negotiate with representatives of the employees, obtaining "yellow dog" contracts, and with the use of labor spies the employer could effectively crush the unionization of his employees. All of these practices became unlawful under the National Labor Relations Act of 1935, and under that Act the Federal Government gave a direct grant of power to employees and their labor unions.

The basic grants of power to employees follow from the preamble to the National Labor Relations Act of 1935 (Section 1), set forth in Appendix B at page 2. The preamble found that individual employees did not "possess full freedom of association or actual liberty of contract" and that "protection by law of the rights of employees to organize and bargain collectively" safeguards commerce; to eliminate obstructions to commerce it was necessary to protect "the exercise by workers of full freedom of association, self organization, and designation of representatives of their own choosing." Section 7 of the National Labor Relations Act of 1935 (Appendix B, p. 3) guaranteed the following rights to employees:

"Employees shall have the right to self-organization, to form, join, or assist labor organizations, to

bargain collectively through representatives of their own choosing, and to engage in concerted activities, for the purpose of collective bargaining or other mutual aid or protection.”

Under Section 9 (a) (Appendix B, p. 3) of the Act representatives designated or selected by the majority of the employees are the exclusive representatives of all employees for the purpose of collective bargaining in respect to rates of pay, wages, hours of employment, or other conditions of employment. Employees are also given the right to enter into a closed shop contract with the employer under the provisions of Section 8 (3) (Appendix B, p. 3).

Under these provisions of the National Labor Relations Act the employee is given the right to designate representatives of his own choosing and these representatives when selected by a majority have exclusive bargaining rights for all members of the class to set the terms and conditions of work. The rights and duties of such a representative have been analyzed and construed by the United States Supreme Court on a number of occasions and, as a result, certain principles have been established which govern the duties of representatives both under the National Labor Relations Act and the Railroad Labor Act, which has comparable provisions. One of those is the principle that powers exercised by the unions are congressionally clothed and comparable to a legislative body. The opinion of Mr. Chief Justice Stone in *Steele v. Louisville and N. R. Co.*, 323 U. S. 192, 65 S. Ct. 226, states:

“Congress has seen fit to clothe the bargaining representatives with powers comparable to those possessed by a legislative body both to create and restrict the rights of those whom it represents, *cf.* J. I. Case

Co. v. National Labor Relations Board, *supra*, 321 U. S. 335, 64 S. Ct. 579, but it has also imposed on the representative a corresponding duty.”

Steele v. Louisville and N. R. Co., 323 U. S. 192, 202, 65 S. Ct. 226, 232.

Another principle established is that the exclusive bargaining agency is the agent of all members of the class whether or not they are members of the bargaining union.

“The duties of a bargaining agent selected under the terms of the Act extend beyond the mere representation of the interests of its own group members. By its selection as bargaining representative, it has become the agent of all the employees, charged with the responsibility of representing their interests fairly and impartially.”

Wallace Corp. v. N. L. R. B., 323 U. S. 248, 255, 65 S. Ct. 238, 241-242.

The union, as bargaining agent, has duties comparable to that of a trustee in its relation to all members of the class which it represents.

“It is to be noted that the seniority rights of Whirls were bargained away from him by a union which, under the National Labor Relations Act, was entitled to bargain as his representative. The Act makes the majority union ‘the exclusive representatives of all the employees in such unit’ for bargaining. 49 Stat. 453, Sec. 9 (a), 29 U. S. C., Sec. 159 (a), 29 U. S. C. A.

“Sec. 159 (a). We have held that this not only precludes the individual from being represented by others but also prevents him from bargaining for himself. *J. I. Case Co. v. National Labor Relations*

Board, 321 U. S. 332, 64 S. Ct. 576, 88 L. Ed. 762. While the individual is thus placed wholly in the power of the union, it does not follow that union powers have no limit. Courts from time immemorial have held that those who undertake to act for others are held to good faith and fair dealing and may not favor themselves at the cost of those they have assumed to represent. The National Labor Relations Act, in authorizing union organizations 'for the purpose of collective bargaining or other mutual aid or protection,' 49 Stat. 452, Sec. 7, 29 U. S. C., Sec. 157, 29 U. S. C. A., Sec. 157, indicates no purpose to excuse unions from these wholesome principles of trusteeship."

Trailmobile Co. v. Whirls, 331 U. S. 40, 67-68, 67 S. Ct. 982, 995, 996 (dissenting opinion of Mr. Justice Jackson).

The only question of law which appears in the decision of the District Judge [Tr. 24-27] is whether the right of the appellant as against the appellees flows to him directly from Section 7 of the National Labor Relations Act of 1935, and under the statutory duties of the union as the exclusive bargaining representative, or whether he claims under some derivative or secondary right as was involved in *Schatte v. International Alliance*, 70 Fed. Supp. 1008, affirmed C. C. A. 9, 165 F. 2d 216 (writ of certiorari denied by Supreme Court). In the *Schatte Case* the plaintiff claimed under a contract which had been entered into pursuant to the National Labor Relations Act, while in this case the appellant has no rights whatsoever if those rights are not given him directly by the National Labor Relations Act; in fact he is claiming rights under the National Labor Relations Act *in the face of* a closed shop contract entered into by the appellee unions.

It is the claim of the appellant that he had offers of employment in the motion picture industry and, in certain instances, was employed by that industry; that appellee unions, although his exclusive bargaining agent under the statute, not only refused to admit him to membership, arbitrarily and without reason, but also refused to permit him to work. Therefore, the appellant says that under the decisions of the Supreme Court of the United States, to be referred to in detail, the unions violated his rights under the National Labor Relations Act by refusing to represent him, refusing to treat him on an equal basis with all other first cameramen in the bargaining unit, refusing to permit him to enter into an individual contract and performing work thereunder, and discriminated against him as his unwilling representative on wages, hours and conditions of employment.

If Congress can clothe a union with exclusive bargaining powers, and a union acting under such powers can by the closed shop contract and refusal to permit qualified persons to membership, prevent employees from contracting for hire, however qualified, then grave constitutional questions arise as to the National Labor Relations Act.

There are many questions of law and interpretations of statutes involved in this case which will be alluded to at a later point in this brief; however, the primary question revolves around the National Labor Relations Act of 1935 and other questions are secondary.

Appellant claims damages for the years beginning 1943 to the date of the filing of the complaint, April 6, 1948, and during most of that period the National Labor Relations Act of 1935 was in force and effect; appellant further alleges that prior to the effective date of the Labor

Management Relations Act of 1947, the appellee unions entered into a closed shop contract which will not expire until December 31, 1948. This closed shop contract is lawful under the Labor Management Relations Act of 1947. Because most of the period concerned is covered by the Act of 1935, and because of the legality of the closed shop contract even under the Labor Management Relations Act of 1947, primary consideration is given to the construction and effect of the 1935 Act, although, so far as venue is concerned, Section 301 (c) of the 1947 Act is set forth in Appendix H, page 18.

Statement of Facts.

The appellant filed his complaint for damages against the appellee unions, International Alliance of Theatrical Stage Employees, etc. ("IATSE"), and International Photographers of the Motion Picture Industry, Local 659 ("Local 659"), and Herbert Aller, its Business Representative. The District Court granted the motions of the appellees to dismiss for lack of jurisdiction and entered its judgment of dismissal for lack of jurisdiction [Tr. 28-29]. For the purposes of considering the propriety of the action of the District Court all of the facts properly pleaded in the complaint are admitted to be true, and therefore we will review these facts in this light.

Appellant alleges that the appellee IATSE and its local unions are labor organizations acting as exclusive bargaining representatives for all employees in the motion picture industry in the State of California who do work in connection with the filming of scenes of motion pictures, including all labor incidental thereto, and who do all preparation, cutting and development of exposed film for shipment into interstate commerce; that Local 659 is a labor

organization composed of first cameramen, and is a local union of the IATSE; that Local 659 represents all first cameramen in the motion picture industry in the State of California and that all employers engaged in the production of motion pictures within such State are under contract with Local 659 for a term ending December 31, 1948, whereby no person may be employed as a first cameraman without membership in Local 659. The complaint also points out that a labor dispute between Local 659 and the employers would burden and obstruct interstate commerce [Tr. 3-8].

The complaint alleges that the majority of exposed film and value of products are produced within the State of California, matters which are of common knowledge, and that the majority of employees are engaged by producers for an individual motion picture, including members of Local 659 [Tr. 9].

Appellant was born in Europe in a portion of the German Empire which subsequently became within the sovereignty of the Republic of Poland, and plaintiff entered the United States under the Polish quota in May of 1941. In July of that same year he filed his declaration of intention to become a citizen and, on the 11th of July, 1947, became a citizen of the United States of America. Appellant, with twenty years' experience, came to this country with an international reputation as first cameraman and this reputation was well known among employers, directors, actors and actresses in the motion picture industry within the State of California. The American Society of Cinemaphotographers, an independent union, was, up until the end of 1942, the exclusive bargaining representa-

tive of first cameramen, and during that period appellant was unable to obtain membership in that labor organization, as well as unable to work as a result [Tr. 9-10].

Ever since January of 1942, plaintiff has applied for membership in Local 659, doing all things required thereunder for membership, and ever since that date Local 659 has arbitrarily and without reason refused him membership, and refused to permit appellant to work as first cameraman for any employer engaged in the production of motion pictures within the State of California. Ever since January 1, 1943, Local 659 has not admitted to membership any first cameraman, although many qualified persons have applied for membership [Tr. 9-11].

During the period that appellant was an alien he was denied membership in the union because of the By-Law of the IATSE that no person who was not a citizen of the United States or Canada could be admitted to membership; after appellant became a citizen the By-Laws of Local 659 provided that no first cameraman should be admitted to the union [Tr. 12-13].

Appellant has continuously, ever since he entered the United States, been offered employment as first cameraman, but, nevertheless, appellees refused to permit him to work with the exception of three motion pictures, and then under conditions that appellant could not look into the camera, touch the camera, nor give any order or direction to the camera crew, and with the additional requirement that appellant's employer hire an extra union first cameraman [Tr. 13-14].

The remaining allegations concern the damages to the appellant [Tr. 15-16].

Appellees moved to dismiss the complaint on the ground of lack of jurisdiction [Tr. 17-21]; the District Judge rendered his decision based on the conclusion that the case was covered by *Schatte v. International Alliance*, 70 Fed. Supp. 1008, affirmed C. C. A. 9, 165 F. 2d 216 (writ of certiorari denied by the Supreme Court) [Tr. 24-27], and rendered his judgment of dismissal for lack of jurisdiction [Tr. 28-29]; the appellant appealed from such final judgment [Tr. 29].

The question is thus squarely presented as to whether or not an alien entering the United States under the protection of a Polish Treaty (Appendix C, p. 4), and subsequently becoming a citizen of the United States of America, has any right to be heard in the Federal Courts when, although he has offers of employment and has been employed in the industry, is prevented from working either with or without a union membership by the exclusive bargaining agency acting under a grant of power from the Congress of the United States, a nation not only bound by its constitutional provisions (Appendix A, p. 1), but also by the Charter of the United Nations (Appendix D, p. 8).

ERROR NO. 1.

The District Court Erred in Rendering a Judgment of Dismissal for Lack of Jurisdiction.

POINTS OF LAW.

I.

The District Court Has Jurisdiction of the Action Under the National Labor Relations Act, the Treaty With Poland, the United Nations Charter and the Express Provisions of the Judicial Code.

A. THE RIGHTS OF APPELLANT AND DUTIES OF APPELLEES UNDER THE NATIONAL LABOR RELATIONS ACT OF 1935.

Appellant claims the basic right guaranteed under Section 7 of the National Labor Relations Act (Appendix B, p. 3) to “join * * * labor organizations” and to “bargain collectively” through representatives of his own choosing; appellant also claims that appellee unions have the duty as appellant’s statutory representative under the National Labor Relations Act to represent him with the same fidelity as other first cameramen and under the National Labor Relations Act to either admit him to membership or permit him to enter into contracts of hire without obstruction. It is the position of appellant that appellee unions by refusing him membership and refusing to permit him to work have violated the duties imposed by the National Labor Relations Act and should respond in damages.

The appellees are acting under a congressional grant of power as the exclusive bargaining agency for all first cameramen, and with such a power they have duties similar to that of a legislature, agent and trustee to act toward appellant without discrimination to the end that he may freely work at his chosen trade.

Steele v. Louisville and N. R. Co., 323 U. S. 192,
65 S. Ct. 226, 89 L. Ed. 173;

Tunstall v. Brotherhood of Locomotive Firemen,
323 U. S. 210, 65 S. Ct. 235, 89 L. Ed. 187;

Wallace Corp. v. N. L. R. B., 323 U. S. 248, 65
S. Ct. 238, 89 L. Ed. 216;

Brotherhood of Locomotive Firemen v. Tunstall
(C. C. A. 4), 163 F. 2d 289;

Graham v. Southern Ry. Co., 74 Fed. Supp. 663;

Betts v. Easley, 161 Kan. 459, 169 P. 2d 831, 166
A. L. R. 342;

James v. Marinship, 25 Cal. 2d 721, 155 P. 2d 329,
160 A. L. R. 900;

Williams v. International Brotherhood, 27 Cal. 2d
586, 165 P. 2d 903;

International Union v. J. I. Case Co., 250 Wis. 63,
26 N. W. 2d 305, 170 A. L. R. 933.

In *Steele v. Louisville and N. R. Co.*, *supra*, the union acted as the exclusive bargaining representative for all employees and made an agreement with the employer that only white employees should be promoted to the better position of fireman or assigned to new runs. The petitioner, a negro, filed a complaint in the State Court and the trial court sustained a demurrer which was affirmed by the Supreme Court of the State. The Supreme Court of the United States reversed the judgment of the State Court and held that the union as exclusive bargaining representative under the Railway Labor Act had a duty to represent all employees whether members or not, and could not arbitrarily discriminate against any member of the group it represented, saying that the union as exclusive bargaining representative had powers not unlike a legislature and therefore was prohibited from discriminating

against anyone for whom it legislates, and that it has a duty to protect the minority of a craft. The Court in the course of its opinion stated:

“If, as the state court has held, the Act confers this power on the bargaining representative of a craft or class of employees without any commensurate statutory duty toward its members, constitutional questions arise. For the representative is clothed with power not unlike that of a legislature which is subject to constitutional limitations on its power to deny, restrict, destroy or discriminate against the rights of those for whom it legislates and which is also under an affirmative constitutional duty equally to protect those rights. If the Railway Labor Act purports to impose on petitioner and the other Negro members of the craft the legal duty to comply with the terms of a contract whereby the representative has discriminatorily restricted their employment for the benefit and advantage of the Brotherhood’s own members, we must decide the constitutional questions which petitioner raises in his pleading.

“But we think that Congress, in enacting the Railway Labor Act and authorizing a labor union, chosen by a majority of a craft, to represent the craft, did not intend to confer plenary power upon the union to sacrifice, for the benefit of its members, rights of the minority of the craft, without imposing on it any duty to protect the minority.

* * * * *

“Unless the labor union representing a craft owes some duty to represent non-union members of the craft, at least to the extent of not discriminating against them as such in the contracts which it makes as their representative, the minority would be left

with no means of protecting their interests, or indeed, their right to earn a livelihood by pursuing the occupation in which they are employed.

“While the majority of the craft chooses the bargaining representative, when chosen it represents, as the Act by its terms makes plain, the craft or class, and not the majority. The fair interpretation of the statutory language is that the organization chosen to represent a craft is to represent all its members, the majority as well as the minority, and it is to act for and not against those whom it represents. It is a principle of general application that the exercise of a granted power to act in behalf of others involves the assumption toward them of a duty to exercise the power in their interest and behalf, and that such a grant of power will not be deemed to dispense with all duty toward those for whom it is exercised unless so expressed.

“We think that the Railway Labor Act imposes upon the statutory representative of a craft at least as exacting a duty to protect equally the interests of the members of the craft as the Constitution imposes upon a legislature to give equal protection to the interests of those for whom it legislates. Congress has seen fit to clothe the bargaining representative with powers comparable to those possessed by a legislative body both to create and restrict the rights of those whom it represents, *cf. J. I. Case Co. v. National Labor Relations Board, supra*, 321 U. S. 335, 64 S. Ct. 579, but it has also imposed on the representative a corresponding duty. We hold that the language of the Act to which we have referred, read in the light of the purposes of the Act, expresses the aim of Congress to impose on the bargaining representative of a craft or class of employees the duty to exercise fairly

the power conferred upon it in behalf of all those for whom it acts, without hostile discrimination against them.

* * * * *

“So long as a labor union assumes to act as the statutory representative of a craft, it cannot rightly refuse to perform the duty, which is inseparable from the power of representation conferred upon it, to represent the entire membership of the craft. While the statute does not deny to such a bargaining labor organization the right to determine eligibility to its membership, it does require the union, in collective bargaining and in making contracts with the carrier, to represent non-union or minority union members of the craft without hostile discrimination, fairly, impartially, and in good faith.”

Steele v. Louisville and N. R. Co., 323 U. S. 192, 198, 199, 201, 202, 203, 204, 65 S. Ct. 226, 230, 231, 232, 233, 89 L. Ed. 173.

The facts in *Tunstall v. Brotherhood of Locomotive Firemen*, *supra*, were similar to *Steele v. Louisville and N. R. Co.*, *supra*, except that in the *Tunstall Case* the action was filed in the Federal District Court instead of the State Court. The United States Supreme Court held that the duty imposed by the Railway Labor Act was a Federal right over which the Federal Courts had jurisdiction under 28 U. S. C. A. 41 (8).

“We also hold that the right asserted by petitioner which is derived from the duty imposed by the Railway Labor Act on the Brotherhood, as bargaining representative, is a federal right implied from the statute and the policy which it has adopted. It is the federal statute which condemns as unlawful the

Brotherhood's conduct. 'The extent and nature of the legal consequences of this condemnation though left by the statute to judicial determination, are nevertheless to be derived from it and the federal policy which it has adopted.' *Deitrick v. Greaney*, 309 U. S. 190, 200, 201, 60 S. Ct. 480, 484, 485, 84 L. Ed. 1036; *Board of Com'rs of Jackson County v. United States*, 308 U. S. 343, 60 S. Ct. 285, 84 L. Ed. 313; *Sola Electric Co. v. Jefferson Electric Co.*, 317 U. S. 173, 176, 177, 63 S. Ct. 172, 173, 174, 87 L. Ed. 165; *cf. Clearfield Trust Co. v. United States*, 318 U. S. 363, 63 S. Ct. 573, 87 L. Ed. 838. The case is therefore one arising under a law regulating commerce of which the federal courts are given jurisdiction by 28 U. S. C. §41(8), 28 U. S. C. A. §41(8), Judicial Code §24(8); * * *

Tunstall v. Brotherhood of Locomotive Firemen, 323 U. S. 210, 213, 65 S. Ct. 235, 237, 89 L. Ed. 187.

In *Wallace Corp. v. N. L. R. B.*, *supra*, one union was certified by the National Labor Relations Board as the exclusive bargaining agency for all employees, and thereupon signed a closed shop contract with the employer, making a demand on the employer that members of the other union who had lost the Board election be discharged. The employer thereupon discharged such employees knowing that they were being excluded from membership in the certified union because of their previous membership in the losing union. The order of the National Labor Relations Board requiring reinstatement of such employees was affirmed by the United States Supreme Court in an opinion by Mr. Justice Black, who said:

"The duties of a bargaining agent selected under the terms of the Act extend beyond the mere repre-

sensation of the interests of its own group members. By its selection as bargaining representative, it has become the agent of all the employees, charged with the responsibility of representing their interests fairly and impartially. Otherwise, employees who are not members of a selected union at the time it is chosen by the majority would be left without adequate representation. No employee can be deprived of his employment because of his prior affiliation with any particular union. The Labor Relations Act was designed to wipe out such discrimination in industrial relations. Numerous decisions of this Court dealing with the Act have established beyond doubt that workers shall not be discriminatorily discharged because of their affiliation with a union. We do not construe the provision authorizing a closed shop contract as indicating an intention on the part of Congress to authorize a majority of workers and a company, as in the instant case, to penalize minority groups of workers by depriving them of that full freedom of association and self-organization which it was the prime purpose of the Act to protect for all workers."

Wallace Corp. v. N. L. R. B., 323 U. S. 248, 255, 256, 65 S. Ct. 238, 241, 242, 89 L. Ed. 216.

After the United States Supreme Court decided *Tunstall v. Brotherhood of Locomotive Firemen*, *supra*, it was remanded to the District Court, which granted to the plaintiff damages against the union (69 Fed. Supp. 826), and upon appeal the judgment was affirmed, the Court saying:

"It is argued that the Brotherhood may not be held liable for damages because it was given a discretion with respect to bargaining and because it is a non-profit organization. No authority is cited to sustain this proposition, and we know of none. No reason

occurs to us why an organization which has used its power as bargaining agent in violation of the rights of those for whom it undertakes to bargain, and has thereby inflicted injury upon one of those whom it professes to represent, should not respond in damages for the injury so inflicted. If liability were thought to be a subject of doubt in such case, we might find helpful analogy in the cases which hold to accountability an agent who has violated the duty which he owes those for whom he acts or in the cases which establish liability for interference with contract. It is not necessary, however, to go to these, as the Supreme Court in the *Steele case*, *supra*, has definitely ruled that such liability exists. See 323 U. S. at page 207, 65 S. Ct. 226, 89 L. Ed. 173."

Brotherhood of Locomotive Firemen v. Tunstall
(C. C. A. 4), 163 F. 2d 289, 293.

In *Graham v. Southern Ry. Co.*, *supra*, members of the negro race were again discriminated against by a railroad union which did not permit them to work diesel engines replacing steam power. The District Court struck down this discrimination; saying:

"We are dealing here with the law regulating the duties of an agent toward his principal. No one is compelled or required to undertake an agency, but one who voluntarily assumes the task owes the duty of acting in the utmost good faith toward his principal. An agent is a fiduciary. If the principal is a group of individuals, this obligation extends to each member of the group. The agent is bound to represent the interest of each member of the group fairly and with equal zeal. He may not neglect some of the members, prefer some as against others, or discriminate among them. He may not advance the interests of some to

the prejudice of others. This is implicit in the fiduciary relationship that exists between every agent and his principal, be that principal a single individual or a group of individuals.

“Applying these general principles to the situation presented in this case, the Brotherhood was under no obligation to become a bargaining agent for the employees within its craft. Having sought to do so, and having been elected to that position of trust, the Brotherhood is in duty bound to represent fairly not only its own membership, but all the employees in whose behalf it has authority to bargain. The Brotherhood must advance equally and in good faith the interests of every individual fireman whom they represent, without preference or discrimination among them. The only permissible distinctions may be those based on seniority, efficiency, reliability, aptitude and similar considerations bearing on the quality of services rendered by the employees. No line may be drawn arbitrarily on any other basis.”

Graham v. Southern Ry. Co., 74 Fed. Supp. 663, 664, 665.

In *Berts v. Easley*, *supra*, the negro workmen sought an injunction against their exclusive bargaining agency under the Railway Labor Act restraining the officers of the union from excluding them from coparticipation with the white employees in the affairs of the union as full members. The Supreme Court of Kansas reversed the judgment of the trial court in sustaining the demurrer, saying:

“In the light of the history and purpose of the Act, as construed in many decisions, the trial court’s view that the acts complained of are solely those of ‘a private association of individuals’ is wholly untenable.

The acts complained of are those of an organization acting as an agency created and functioning under provisions of Federal law. This being true, it is unnecessary to consider appellees' contention that the Fifth Amendment is not here applicable because it relates only to action by the Federal government and not to acts of private persons. Nor do we need to inquire whether appellees' statement as to the operation of the Fifth Amendment is too broadly stated. In any event the constitutional guaranties of due process, whether under the Federal or state constitutions, are to be liberally construed to effectuate their purposes, and are a restraint not only upon persons holding positions specifically classed as executive, legislative or judicial, but upon all administrative and ministerial officials who act under governmental authority. 16 C. J. S., Constitutional Law, §568, pp. 1148, 1149, and cases cited Note 61. While claiming and exercising rights incident to its designation as bargaining agent, the defendant union cannot at the same time avoid the responsibilities that attach to such statutory status.

* * * * *

"It is urged, however, that since membership in the union is voluntary and not compulsory, the petitioners have no right to complain about limitations placed upon membership under the constitution and by-laws of the union. The argument is specious and unrealistic. Note might here be taken of the allegation that in soliciting members, prior to organization of the local lodge, the organizer assured the plaintiffs that all members would have equal rights and privileges. But passing that, we come to a more fundamental matter. This court cannot be blind to present-day realities affecting labor in large industrial plants.

The individual workman cannot just 'go it alone.' Every person with an understanding of mass production and other features of modern industry long ago recognized the necessity of collective bargaining by labor representatives, freely chosen, if human rights are to be adequately safeguarded. In the Railway Labor Act, Congress gave clear and firm recognition to this necessity. This liberal and enlightened view having been written into the statute, it must follow that a union acting as the exclusive bargaining agent under the law, for all employees, cannot act arbitrarily, cannot deny equality of privilege, to individuals or minority groups merely because membership in the organization is voluntary. To hold otherwise would do violence to basic principles of our American system."

Betts v. Easley, 161 Kan. 459, 169 P. 2d 831, 166 A. L. R. 342, 350, 351.

In *James v. Marinship*, *supra*, and *Williams v. International Brotherhood*, *supra*, the California Supreme Court in carefully considered opinions has set forth the duties of the collective bargaining agency. Not even a contract between an employer and a union whereby certain individual employees are excluded from its benefits is valid under the National Labor Relations Act. (*International Union v. J. I. Case Co.*, *supra*.) The Court in that case held a contract invalid between a union and an employer where there was reserved to employees not members of the union a right to deal individually with the company. The Court said:

" 'Exclusive representatives' for the purpose of collective bargaining under the Act means the sole and exclusive bargaining agency of all the employees it

represents for the purpose of bargaining as to rates of pay, wages, hours of employment, or other conditions of employment.

* * * * *

“The company cannot by contract destroy the status of an exclusive bargaining agency created by statute. The terms of the contract being in direct conflict with the statute, the statute governs, and the contract is of no effect.”

International Union v. J. I. Case Co., 250 Wis. 63,
26 N. W. 2d 305, 170 A. L. R. 933, 939.

The appellant had numerous offers of employment and was employed for three motion picture productions as first cameraman. He has applied for membership in the appellee unions and has designated them as his exclusive bargaining representatives under the applications. The appellee unions, by virtue of statute, are his exclusive bargaining agents on wages, hours and working conditions. It is the contention of appellant that the unions, in preventing him from working and refusing him membership, have violated their duty to him under the following principles: “For the representative is clothed with power not unlike that of a legislature which is subject to constitutional limitations on its power to deny, restrict, destroy or discriminate against the rights of those for whom it legislates and which is also under an affirmative constitutional duty equally to protect those rights.” (*Steele v. Louisville and N. R. Co.*, *supra*.) The statute “does require the union, in collective bargaining and in making contracts with the carrier, to represent non-union or minority union members of the craft without hostile discrimination, fairly, impartially, and in good faith.” (*Steele v. Louisville and*

N. R. Co., supra.) "It is the federal statute which condemns as unlawful the Brotherhood's conduct." (*Tunstall v. Brotherhood of Locomotive Firemen, supra.*) "By its selection as bargaining representative, it has become the agent of all the employees, charged with the responsibility of representing their interests fairly and impartially. Otherwise, employees who are not members of a selected union at the time it is chosen by the majority would be left without adequate representation." (*Wallace Corp. v. N. L. R. B., supra.*) "No reason occurs to us why an organization which has used its power as bargaining agent in violation of the rights of those for whom it undertakes to bargain, and has thereby inflicted injury upon one of those whom it professes to represent, should not respond in damages for the injury so inflicted." (*Brotherhood of Locomotive Firemen v. Tunstall, supra.*) "An agent is a fiduciary. If the principal is a group of individuals, this obligation extends to each member of the group." (*Graham v. Southern Ry. Co., supra.*) "The individual workman cannot just 'go it alone.' Every person with an understanding of mass production and other features of modern industry long ago recognized the necessity of collective bargaining by labor representatives, freely chosen, if human rights are to be adequately safeguarded." (*Betts v. Easley, supra.*)

It is therefore under these principles that appellant asks the Federal Court to take jurisdiction of this controversy with appellee unions.

The Federal District Court had jurisdiction of this case under 28 U. S. C. A. 41 (1) (now 28 U. S. C. A. 1331) (Appendix E, p. 12), where the matter in controversy exceeds \$3,000.00 and arises under the Constitution, laws or treaties of the United States, as well as under former

28 U. S. C. A. 41 (8) (now 28 U. S. C. A. 1337), which gives jurisdiction to proceedings arising under any law regulating commerce.

Tunstall v. Brotherhood of Locomotive Firemen,
323 U. S. 210, 65 S. Ct. 235, 89 L. Ed. 187.

There is no allegation in the complaint and appellant does not claim that there is any jurisdiction based on the amount in controversy and diversity of citizenship. So far as this subpoint in his argument is concerned, he relies wholly on jurisdiction of the District Court under the laws of the United States and the National Labor Relations Act, being an Act of Congress regulating commerce.

B. APPELLANT, A CITIZEN OF THE REPUBLIC OF POLAND, WAS, BY THE TREATY BETWEEN THE UNITED STATES AND POLAND OF FRIENDSHIP, ETC., GUARANTEED CERTAIN RIGHTS DENIED HIM BY APPELLEES.

Under the decided cases, the treaty between the United States and Poland of Friendship, Commerce and Consular Rights (Appendix C, p. 4) guaranteed to appellant the rights accorded nationals of Poland under that treaty. These rights, among others, were "to engage in * * * commercial work of every kind; * * * to employ agents of their choice; and generally * * * to enjoy all of the foregoing privileges and to do anything incidental to or necessary for the enjoyment of those privileges, upon the same terms as nationals of the State of residence * * *. Their property shall not be taken without due process of law * * *. The nationals * * * shall enjoy * * * such rights and privileges as have been or may hereafter be accorded the nationals of any other State with respect to the organization of

and participation in limited liability and other corporations and associations, for pecuniary profit or otherwise, * * *.” (Appendix C, p. 4.)

Under similar treaties between the United States and other countries, the Supreme Court has held without any question as to whether or not treaties are self-executing, that the nationals of the other countries were entitled to work without restraint by state action.

Yick Wo. v. Hopkins, 118 U. S. 356, 6 S. Ct. 1064, 30 L. Ed. 220;

Truax v. Raich, 239 U. S. 33, 36 S. Ct. 7, 60 L. Ed. 131.

An excellent exposition of the established principles concerning treaties is found in *Z. & F. Assets Realization Corporation v. Hull* (D. C. App.), 114 F. 2d 464 (affirmed 311 U. S. 470, 61 S. Ct. 351, 85 L. Ed. 288):

“A treaty is primarily a compact between independent nations. It depends for the enforcement of its provisions on the interest and the honor of the governments which are parties to it. If these fail, its infraction becomes the subject of international negotiations and reclamations, so far as the injured party chooses to seek redress, which may in the end be enforced by actual war. It is obvious that with all this the judicial courts have nothing to do and can give no redress. But a treaty may also contain provisions which confer certain rights upon the citizens or subjects of one of the nations residing in the territorial limits of the other, which partake of the nature of municipal law, and which are capable of enforcement as between private parties in the courts of the country. An illustration of this character is found in treaties, which regulate the mutual rights of citizens and sub-

jects of the contracting nations in regard to rights of property by descent or inheritance, when the individuals concerned are aliens. The Constitution of the United States places such provisions as these in the same category as other laws of Congress by its declaration that 'this Constitution and the laws made in pursuance thereof, and all treaties made or which shall be made under authority of the United States, shall be the supreme law of the land.' A treaty, then, is a law of the land as an act of Congress is, whenever its provisions prescribe a rule by which the rights of the private citizen or subject may be determined. And when such rights are of a nature to be enforced in a court of justice, that court resorts to the treaty for a rule of decision for the case before it as it would to a statute."

Z. & F. Assets Realization Corporation v. Hull
(D. C. App.), 114 F. 2d 464, 470, 471.

The principles laid down by the Court in the *Z. & F. Assets* case have been established over a long period of time.

Edye v. Robertson, 112 U. S. 580, 5 S. Ct. 247, 28 L. Ed. 798;

Foster v. Neilson, 2 Pet. 253, 314, 7 L. Ed. 415, 435;

U. S. v. Percheman, 7 Pet. 51, 8 L. Ed. 604;

The Peggy, 1 Cranch 103, 2 L. Ed. 49;

U. S. v. 43 Gallons Whisky, 93 U. S. 188, 23 L. Ed. 846;

Indemnity Ins. Co. v. Pan Am. Airways (D. C. N. Y.), 58 Fed. Supp. 338;

Holden v. Joy, 17 Wall. 211, 21 L. Ed. 523, 535;

Hines v. Davidowitz, 312 U. S. 52, 61 S. Ct. 399, 85 L. Ed. 581;

Valentine v. U. S., 299 U. S. 5, 57 S. Ct. 100, 81 L. Ed. 5;

King Features Syndicate v. Valley Broadcasting Co. (D. C. Tex.), 43 Fed. Supp. 137;

Cook v. U. S., 288 U. S. 102, 53 S. Ct. 305, 77 L. Ed. 641;

Bacardi Corp. v. Domenech, 311 U. S. 150, 61 S. Ct. 219, 85 L. Ed. 98.

Mr. Chief Justice Marshall in *Foster v. Neilson*, *supra*, said:

“Our Constitution declares a treaty to be the law of the land. It is, consequently, to be regarded in courts of justice as equivalent to an Act of the Legislature, whenever it operates of itself without the aid of any legislative provision. But when the terms of the stipulation import a contract—when either of the parties engages to perform a particular act—the treaty addresses itself to the political, not the judicial department; and the Legislature must execute the contract before it can become a rule for the court.”

Foster v. Neilson, 2 Pet. 253, 314, 7 L. Ed. 415, 435.

In *Asakura v. Seattle*, 265 U. S. 332, 44 S. Ct. 515, 68 L. Ed. 1041, the Court held that the treaty with Japan containing similar provisions as the Polish Treaty was self-executing and that an ordinance limiting the right of pawnbrokers to carry on business to persons who were citizens of the United States was void as a violation of the treaty with Japan.

Special rights of a person who has filed his declaration to become a citizen are considered in *Terrace v. Thompson*, 263 U. S. 197, 220, 68 L. Ed. 255, 276, 44 S. Ct. 15.

It is apparent under the cases above cited that appellant, if deemed to have no special rights as one who had filed his declaration to become a citizen, is entitled up to the time when he became a citizen, to rely upon the Polish Treaty which was self-executing and under which he was entitled to engage in commercial work, to appoint agents, to have the equal protection of the laws, and to join associations. Therefore, when the appellees, as exclusive bargaining agency under the National Labor Relations Act, deny him these rights, this Court has jurisdiction under 28 U. S. C. A. 41 (17) (now 28 U. S. C. A. 1350) (Appendix E, p. 14), which permits an alien to file an action in the Federal Courts for a tort arising out of a treaty as well as under 28 U. S. C. A. 41 (1), now 28 U. S. C. 1331.

C. THE APPELLANT CLAIMS UNDER RIGHTS GUARANTEED BY THE UNITED NATIONS CHARTER.

Appellees in the course of their brief in the District Court set forth an ultimate statement concerning the fundamental rights of the appellant, which we take the privilege of quoting at this point:

“That the right to follow any of the common occupations of life and to pursue any calling, business or profession one may choose is a property right to be guarded by the proper Courts as zealously as any other form of property, that labor is property and

that the laborer has the same right to sell his labor and to contract with reference thereto as any other property owner, cannot be questioned. Such rights are natural, fundamental, inalienable rights; they exist in all free governments.”

Appellees, of course, went on to state that these rights were not protected by the Constitution of the United States or any statute or law of the United States. However, they neglected to consider the United Nations Charter. These rights which appellees say “exist in all free governments” are also guaranteed by the Constitution of the United States, as we will subsequently point out under Point III. The United Nations Charter (Appendix D, p. 8) uses almost the identical words of the appellee unions as above set forth. In the Preamble the peoples of the United Nations reaffirm their faith in “fundamental human rights, in the dignity and worth of the human person, in the equal rights of men and women and of nations large and small; * * *” The purposes of the United Nations are to achieve international cooperation in “promoting and encouraging respect for human rights and for fundamental freedoms for all; * * *” (Chapter I, Article 1, Paragraph 3.) Article 2 provides that members shall fulfill the obligations assumed by them in accordance with the purposes stated in Article 1, and Article 55 again reemphasizes these principles which, under Article 56, members are obliged to take joint and separate action to achieve.

While the Charter of the United Nations was only adopted in 1945, nevertheless four Justices of the Supreme

Court in the *Alien Land Law* case have concluded that it is applicable to the internal affairs of the United States.

Oyama v. State of California, 332 U. S. 633, 68 S. Ct. 269 (the *Opinion of Mr. Justice Black*, 68 S. Ct. at 277; the *Opinion of Mr. Justice Murphy*, 68 S. Ct. at 288).

Mr. Justice Black said:

“There are additional reasons now why that law stands as an obstacle to the free accomplishment of our policy in the international field. One of these reasons is that we have recently pledged ourselves to cooperate with the United Nations to ‘promote * * * universal respect for, and observance of, human rights and fundamental freedoms for all without distinction as to race, sex, language, or religion.’ How can this nation be faithful to this international pledge if state laws which bar land ownership and occupancy by aliens on account of race are permitted to be enforced?”

Oyama v. State of California, 332 U. S. 633, 68 S. Ct. 269, at 277.

Mr. Justice Murphy said:

“Moreover, this nation has recently pledged itself, through the United Nations Charter, to promote respect for, and observance of, human rights and fundamental freedoms for all without distinction as to race, sex, language and religion. The Alien Land Law stands as a barrier to the fulfillment of that national pledge. Its inconsistency with the Charter, which has been duly ratified and adopted by the United States, is but one more reason why the statute must be condemned.”

Oyama v. State of California, 332 U. S. 633, 68 S. Ct. 269, at 288.

Therefore, under the Charter of the United Nations establishing human, fundamental and natural rights which the appellees admit "exist in all free Governments" with the pledge of the United States as contained in the Charter to carry out its purposes, the appellant can rely on the Federal Courts to carry out their constitutional duties to make effective his rights under this treaty.

II.

Under the National Labor Relations Act, Congress Has Clothed Appellees With an Exclusive Franchise, and Under the Act and the Common Law Applicable Thereto, Appellees Have Violated Their Duty Toward Appellant, a Federal Question.

The Supreme Court of the United States has set forth the powers of unions under the National Labor Relations Act. The employer was not only required to negotiate with the union as the exclusive bargaining agency of its employees, but also the Act imposed the "negative duty to treat with no other."

N. L. R. B. v. Jones & Laughlin Steel Corporation,
301 U. S. 1, 57 S. Ct. 615, 81 L. Ed. 893.

Not only was the employer to deal with the exclusive bargaining representative, and with no other union, but also he could not make any individual contract with an employee except the original contract of hire.

J. I. Case Co. v. N. L. R. B., 321 U. S. 332, 64 S. Ct. 576, 88 L. Ed. 762.

Under these decisions the individual or minority group can make no contract for themselves, but must accede to the will of the statutory representatives of the majority.

This power of exclusive representation on the part of the unions is in the nature of an exclusive franchise or monopoly which has been granted under governmental authority. Therefore, under this exclusive franchise, the appellee unions must treat all without discrimination in accordance with the long established principles of common law.

Munn v. Illinois, 94 U. S. 113, 24 L. Ed. 77;

Stafford v. Wallace, 258 U. S. 495, 66 L. Ed. 735, 42 S. Ct. 397;

U. S. v. Ohio Oil Co., 234 U. S. 548, 58 L. Ed. 1459, 34 S. Ct. 956;

Slaughter House Cases, 16 Wall. 36, 21 L. Ed. 394, 425;

The York Manufacturing Co. v. The Illinois Central Railroad, 3 Wall. 107, 112, 18 L. Ed. 170, 172, 70 U. S. 170;

Missouri Pac. Rwy. Co. v. Tucker, 230 U. S. 340, 33 S. Ct. 961, 57 L. Ed. 1507;

4 R. C. L. 565, 9 Am. Jur. 556.

Where unions have obtained monopolies by the closed shop and the closed union, the State Courts have universally regulated those unions if the unions refused to admit qualified persons to membership.

Wilson v. Newspaper & Mail Deliverers' Union, 123 N. J. Eq. 347, 197 Atl. 720;

Carroll v. Local No. 269, I. B. E. W., 133 N. J. Eq. 144, 31 A. 2d 223;

Dorrington v. Manning (Pa. Super.), 4 A. 2d 886;

James v. Marinship, 25 Cal. 2d 721, 155 P. 2d 329, 160 A. L. R. 900;

Swab v. Motion Picture Machine Operators Local No. 159 (Ore.), 109 P. 2d 600;

Restatement, Torts, Secs. 810, 918.

Thus it would appear under the authorities cited above that where a union was acting under its statutory exclusive bargaining agency and where it has obtained a closed shop contract under the permission set forth in Section 8 of the National Labor Relations Act, the union had the duty to admit all persons to its union who were qualified workers and who were able to obtain contracts of employment. It would also appear that the right of such persons to join labor organizations has been granted under Section 7 of the National Labor Relations Act; this is essential in order that persons employed in an industry may take part in the affairs of the union. But, assuming for the purposes of argument that appellant has no right to join the appellee unions, nevertheless, the appellees acting as the exclusive bargaining agency for all first cameramen, including appellant, should have made provision whereby appellant could work without membership in the union, which was required of them as his designated representative. Finally the appellee acting under their exclusive franchise granted to them by the Congress at least owed the duty to the appellant not to interfere with his working as first cameraman.

III.

If, Acting Under Congressional Authority, Appellees Have the Right to Prevent Appellant From Entering Into a Contract of Hire, Then Grave Questions of the Constitutionality of the National Labor Relations Act Arise, a Federal Question.

The Fifth and Fourteenth Amendments to the Constitution of the United States provide that no person shall be deprived of life, liberty or property without due process of law, and restrain respectively the State and Federal Governments and their agencies from any violations of the rights guaranteed by these Amendments to the Constitution.

Appellant says that the National Labor Relations Act cannot be construed to take away his right to enter into a contract of hire, the only privilege left to him under that Act (*J. I. Case Co. v. N. L. R. B.*, 321 U. S. 332, 64 S. Ct. 576, 88 L. Ed. 762); that appellees, either as a Congressionally clothed legislative body or functioning under the Congressional grant of an exclusive franchise, or as statutory agent, cannot take away this right of the appellant. Furthermore, there is the Constitutional duty of the Federal Courts to protect appellant in his right to enter into a contract of hire under the implications of the *Race Restriction Cases*, 334 U. S. 1, 68 S. Ct. 836.

Whether appellant be considered an alien, or having a special status as one who has filed his declaration to become a citizen, or as a white citizen, his rights are protected under the Fifth Amendment to the Constitution.

Yick Wo v. Hopkins, 118 U. S. 356, 6 S. Ct. 1064, 30 L. Ed. 220;

Truax v. Raich, 239 U. S. 33, 36 S. Ct. 7, 60 L. Ed. 131;

Buchanan v. Warley, 245 U. S. 60, 38 S. Ct. 16, 62 L. Ed. 149.

It is immaterial to appellant whether it be determined that his liberty *or* his property has been taken without due process, or whether the Fifth Amendment be construed as guaranteeing him a right to work, a right to enter into a contract, or a right to earn a living. All he desires is a protection from the unlawful interference of others of the right to accept an offer of employment. The Supreme Court and our State Courts have construed the Fifth and Fourteenth Amendments by upholding this right of the appellant.

Yick Wo v. Hopkins, *supra*;

Truax v. Raich, *supra*;

Mitchell v. Hitchman Coal and Coke Co. (C. C. A. 4), 214 Fed. 685, 699 (reversed on other grounds, 245 U. S. 229, 38 S. Ct. 65, 62 L. Ed. 260);

Adams v. Tanner, 244 U. S. 590, 37 S. Ct. 662, 61 L. Ed. 1336, L. R. A. 1917F 1163, Ann. Cas. 1917D 973;

Allgeyer v. Louisiana, 165 U. S. 578, 17 S. Ct. 427, 41 L. Ed. 832;

Chicago B. & Q. R. Co. v. McGuire, 219 U. S. 549, 31 S. Ct. 259, 55 L. Ed. 328;

Booth v. Illinois, 184 U. S. 425, 22 S. Ct. 425, 46 L. Ed. 623.

See:

West Coast Hotel Co. v. Parrish, 300 U. S. 379, 57 S. Ct. 578, 81 L. Ed. 703;

Bautista v. Jones, 25 Cal. 2d 746, 155 P. 2d 343;

Betts v. Easley, 161 Kans. 459, 169 P. 2d 831, 166 A. L. R. 342;

DeMille v. A. F. R. A., 31 Cal. 2d 139 (Cert. denied by U. S. Supreme Court);

Slaughter House Cases, 16 Wall. 36, 21 L. Ed. 394, 425.

In the *Yick Wo* case, *supra*, the Court said:

“For, the very idea that one man may be compelled to hold his life, or the means of living, or any material right essential to the enjoyment of life, at the mere will of another, seems to be intolerable in any country where freedom prevails, as being the essence of slavery itself.”

Yick Wo v. Hopkins, 118 U. S. 356, 6 S. Ct. 1064, 30 L. Ed. 220, 226.

And so in *Truax v. Raich*, *supra*:

“It requires no argument to show that the right to work for a living in the common occupations of the community is of the very essence of the personal freedom and opportunity that it was the purpose of the Amendment to secure.”

Truax v. Raich, 239 U. S. 33, 41, 36 S. Ct. 7, 60 L. Ed. 131, 135.

In *Adams v. Tanner*, *supra*, an initiative measure of the State of Washington prohibited employment agencies from charging any fees and it was held a taking without due process. Opinion by Mr. Justice McReynolds:

“‘You take my house when you do take the prop that doth sustain my house; you take my life when you take the means whereby I live.’” (Shylock—‘*Merchants of Venice*’ Act IV, Scene I, line 376.)

Adams v. Tanner, 244 U. S. 590, 593, 37 S. Ct. 662, 61 L. Ed. 1336, 1342.

In *Allgeyer v. Louisiana*, *supra*, the Court said:

“The liberty mentioned in that amendment means, not only the right of the citizen to be free from the mere physical restraint of his person, as by incarceration, but the term is deemed to embrace the right of the citizen to be free in the enjoyment of all his faculties; to be free to use them in all lawful ways; to live and work where he will; to earn his livelihood by any lawful calling; to pursue any livelihood or avocation, and for that purpose to enter into all contracts which may be proper, necessary, and essential to his carrying out to a successful conclusion the purposes above mentioned.”

Allgeyer v. Louisiana, 165 U. S. 578, 589, 17 S. Ct. 427, 41 L. Ed. 832, 835.

The Court said in *Chicago B. & Q. R. Co. v. McGuire*, *supra*:

“Liberty implies the absence of arbitrary restraint, not immunity from reasonable regulations and prohibitions imposed in the interests of the community.”

Chicago B. & Q. R. Co. v. McGuire, 219 U. S. 549, 567, 31 S. Ct. 259, 55 L. Ed. 328, 338.

In *West Coast Hotel Co. v. Parrish*, *supra*, Mr. Chief Justice Hughes said:

“The constitutional provision invoked is the due process clause of the Fourteenth Amendment governing the States, as the due process clause invoked in the Adkins Case governed Congress. In each case the violation alleged by those attacking minimum wage regulation for women is deprivation of freedom of contract. What is this freedom? The Constitution does not speak of freedom of contract. It speaks of liberty and prohibits the deprivation of

liberty without due process of law. In prohibiting that deprivation the Constitution does not recognize an absolute and uncontrollable liberty. Liberty in each of its phases has its history and connotation. But the liberty safeguard is liberty in a social organization which requires the protection of law against the evils which menace the health, safety, morals and welfare of the people. Liberty under the Constitution is thus necessarily subject to the restraints of due process, and regulation which is reasonable in relation to its subject and is adopted in the interests of the community is due process."

West Coast Hotel Co. v. Parrish, 300 U. S. 379, 391, 57 S. Ct. 578, 81 L. Ed. 703, 708.

And in *Bautista v. Jones*, *supra*, the Court said:

"The right to work, either in employment or independent business, is fundamental and, no doubt, enjoys the protection of the personal liberty guarantee of the Fourteenth Amendment to the federal Constitution, as well as the more specific provisions of our state Constitution. (Cal. Const., art. I, §§1, 13; see *Suckow v. Alderson*, 182 Cal. 247 (187 P. 965); *Angelopoulos v. Bottorff*, 76 Cal. App. 621 (245 P. 447).) But this right, like others equally fundamental, is not absolute. It is safeguarded from legislative action which discriminates against a person or class of persons in respect of opportunities to obtain work or enter into business (*Yick Wo v. Hopkins*, 118 U. S. 356 (6 S. Ct. 1064, 30 L. Ed. 220); *Abe v. Fish & Game Commission*, 9 Cal. App. 2d 300 (49 P. 2d 608)); and it is also protected in some degree

against arbitrary action by private organizations, including employers and labor unions. (*James v. Mar-
inship Corp.*, *supra.*)”

Bautista v. Jones, 25 Cal. 2d 746, 749, 155 P. 2d
343.

Mr. Justice Swayne in his dissenting opinion in the *Slaughter House* cases, *supra*, has aptly expressed what the plaintiff is attempting to say in this case:

“Life, liberty and property are forbidden to be taken ‘without due process of law,’ and ‘equal protection of the laws,’ is guaranteed to all. Life is the gift of God, and the right to preserve it is the most sacred of the rights of man. Liberty is freedom from all restraints but such as are justly imposed by law. Beyond that line lies the domain of usurpation and tyranny. Property is everything which has an exchangeable value, and the right of property includes the power to dispose of it according to the will of the owner. Labor is property, and as such merits protection. The right to make it available is next in importance to the rights of life and liberty. It lies to a large extent at the foundation of most other forms of property, and of all solid individual and national prosperity.”

Slaughter House Cases, 16 Wall. 36, 21 L. Ed. 394
at page 425.

Therefore if, under the National Labor Relations Act the appellees can take away appellant’s right to enter into a contract of employment there must be serious doubts as to the constitutionality of this statute.

IV.

Appellant Claims Rights Under the National Labor Relations Act, the Statutes, Treaties and Laws of the United States; the District Court Has Jurisdiction to Determine Whether or Not Appellant Has Any Rights Under Such Laws.

Under the preceding points of law the appellant has relied on rights under Section 7 of the National Labor Relations Act, on the duties of the appellee unions as exclusive bargaining representatives under the same Act, rights claimed under the Treaty with Poland and the Charter of the United Nations, the common law rights against arbitrary action by the appellee unions, holders of an exclusive franchise under the Federal Government, and the Constitution of the United States.

As stated earlier in this brief, the only question before this Court is whether these claims of Federal rights are substantial, and whether or not the appellant can ultimately establish rights in his favor under these laws of the United States merely goes to the merits of the case and is not involved in this appeal.

This principle was reiterated in the case of *American Federation of Labor v. Watson*, 327 U. S. 582, 66 S. Ct. 761, 90 L. Ed. 873, where Mr. Justice Douglas stated:

“For it is the view of a majority of the Court that jurisdiction is found in Sec. 24 (8) of the Judicial Code, 28 U. S. C. Sec. 41 (8), 28 U. S. C. A. Sec. 41 (8), which grants the federal district courts jurisdiction of all ‘suits and proceedings arising under any law regulating commerce.’ As we have said, the bill alleges a conflict between the Florida law and the National Labor Relations Act. The theory of the bill is that labor unions, certified as collective bargaining

representatives of employees under that Act, are granted as a matter of federal law the right to use the closed-shop agreement or, alternatively, that the right of collective bargaining granted by that Act includes the right to bargain collectively for a closed shop. Whether that claim is correct is a question which goes to the merits. It is, however, a substantial one. And since the right asserted is derived from or recognized by a federal law regulating commerce, a majority of the Court conclude that a suit to protect it against impairment by state action is a suit 'arising under' a federal law 'regulating commerce.' Cf. *Mulford v. Smith*, 307 U. S. 38, 46, 59 S. Ct. 648, 651, 83 L. Ed. 1092; *Peyton v. Railway Express Agency*, 316 U. S. 350, 62 S. Ct. 1171, 86 L. Ed. 1525; *Parker v. Brown*, 317 U. S. 341, 349, 63 S. Ct. 307, 312, 87 L. Ed. 315; *Tunstall v. Brotherhood*, 323 U. S. 210, 213, 65 S. Ct. 235, 237."

American Federation of Labor v. Watson, 327 U. S. 582, at 591, 66 S. Ct. 761, at 765; 90 L. Ed. 873.

The only question is whether appellant relies on direct rights guaranteed by Federal law, or merely indirect and derivative rights.

Gulley v. First National Bank, 299 U. S. 109, 57 S. Ct. 96, 81 L. Ed. 70.

The silence of Congress as to judicial review which is not found in the Act itself is

"not to be construed as a denial of authority to the aggrieved person to seek appropriate relief in the federal courts in the exercise of their general jurisdiction."

Stark v. Wickard, 321 U. S. 288, 309, 64 S. Ct. 559, 571, 88 L. Ed. 733.

V.

Appellant Is an Employee as Defined by the National Labor Relations Act; Has Been Employed as First Cameraman and Has Had Offers of Employment. Appellees Are Estopped From Claiming Appellant Is Not an Employee.

Appellant was a first cameraman for three different employers in the motion picture industry and thereby became a member of the labor pool for first cameramen in that industry. The National Labor Relations Board on many occasions has recognized that, as alleged in the complaint, employment in the motion picture industry is often of an intermittent nature because persons are hired only for the duration of a particular production. This fact was recognized in the certification proceedings for the IATSE, as referred to in paragraph IV of the complaint on file herein and cited as 14 N. L. R. B. 224 [Tr. 6]. The N. L. R. B. did not require as a condition of eligibility that persons be employed on a particular date, which is its usual practice, but ordered that persons working so many days in a year were eligible to vote. Furthermore, Section 2 of the Act provides that the term, "employee" shall include "any employee and shall not be limited to the employees of a particular employer, * * *."

The National Labor Relations Board has also held that free-lance artists are employed within the meaning of the Act and their status is the same as that of employees regularly employed.

K. M. O. X. Broadcasting Station, 10 N. L. R. B. 479.

This principle that where an employee has entered the labor pool and been employed in an industry in which the union is the exclusive bargaining agency certified for

many employers, particularly where employment is intermittent, is in accord with the principles established by the Supreme Court that the National Labor Relations Act contains a broad social program for the benefit of workers as that term is understood, and rights guaranteed thereunder are not limited to the technical relationship of employer-employee, as construed by the law Courts.

Phelps Dodge Corp. v. N. L. R. B., 313 U. S. 177,
61 S. Ct. 845, 85 L. Ed. 1271, 133 A. L. R. 1217;
N. L. R. B. v. Hearst Publications, 322 U. S. 111,
64 S. Ct. 851, 88 L. Ed. 1170.

In the *Phelps Dodge Corp.* case, *supra*, the employer refused to give employment to certain persons because they were members of the union. The order of the National Labor Relations Board which required such persons to be placed on the job was affirmed by the Supreme Court. Mr. Justice Frankfurter, who delivered the opinion, said:

“Discrimination against union labor in the hiring of men is a dam to self organization at the source of supply. The effect of such discrimination is not confined to the actual denial of employment; it inevitably operates against the whole idea of the legitimacy of organization. * * *

“Unlike mathematical symbols, the phrasing of such social legislation as this seldom attains more than approximate precision of definition.”

Phelps Dodge Corp. v. N. L. R. B., 313 U. S. 177,
185, 61 S. Ct. 845, 848, 85 L. Ed. 1271.

In *N. L. R. B. v. Hearst Publications, supra*, the Supreme Court thrust aside the employer's contention that newsboys were independent contractors and not within the coverage of the Act, saying:

"Congress, on the one hand, was not thinking solely of the immediate technical relation of employer and employee. * * *"

"Congress was not seeking to solve the nationally harassing problems with which the statute deals by solutions only partially effective. It rather sought to find a broad solution, one that would bring industrial peace by substituting, so far as its power could reach, the rights of workers to self-organization and collective bargaining for the industrial strife which prevails where these rights are not effectively established. Yet only partial solutions would be provided if large segments of workers about whose technical legal position such local differences exist should be wholly excluded from coverage by reason of such differences."

N. L. R. B. v. Hearst Publications, 322 U. S. 111, 124, 125, 64 S. Ct. 851, 857, 858, 88 L. Ed. 1170.

If further analogy be needed to justify protection for the appellant in this case, the broad program of the National Labor Relations Act should not exclude from its beneficent purposes that person who has one foot in the door of employment and an offer of employment in hand. Appellant certainly has been ever since arrival, a "prospective employee." Courts have held that in the absence of any statute an employee who has struck and whose employer has attempted to terminate the relation of employment, is a "striking employee."

“We believe that *in the absence of statute* the relationship of employer and employee is not completely terminated by a strike, but that a new status arises. The courts have coined a word to describe the situation and have called an employee on strike a ‘striking employee.’” (Emphasis ours.)

N. L. R. B. v. Carlisle Lumber Co. (C. C. A. 9),
94 F. 2d 138, 144.

The appellees admit in their Motion to Dismiss that their actions have prevented the plaintiff from being an employee and yet, at the same time in the District Court, attempted to avoid their responsibilities to the appellant by saying that he is not an employee. The appellees are “blowing hot and cold.” Throughout our common law it has been one of the foundations of our philosophy of justice that a person cannot take advantage of his own wrong. This is also a rule of the Federal Court in considering the construction and application of a Congressional statute.

“It is a principle of the widest application that equity will not permit one to rely on his own wrongful act, as against those affected by it but who have not participated in it, to support his own asserted legal title or to defeat a remedy which except for his misconduct would not be available.”

Deitrick v. Greaney, 309 U. S. 190, 196, 60 S. Ct. 480, 483, 84 L. Ed. 694.

Appellees are in the same position as a common carrier who, when refusing to accept shipment of goods, claims that the person offering the shipment is not a “shipper” because the carrier prevented him from placing his goods on board.

Ohio Tank Car Co. v. Keith Ry. Equipment Co.
(C. C. A. 7), 148 F. 2d 4, 7.

Under the definition of “employee” in Section 2 of the National Labor Relations Act and under the construction of that word by the National Labor Relations Board and the Supreme Court, appellant is an employee within the meaning of the Act; if for any reason he is not, the appellees are not the ones to assert it.

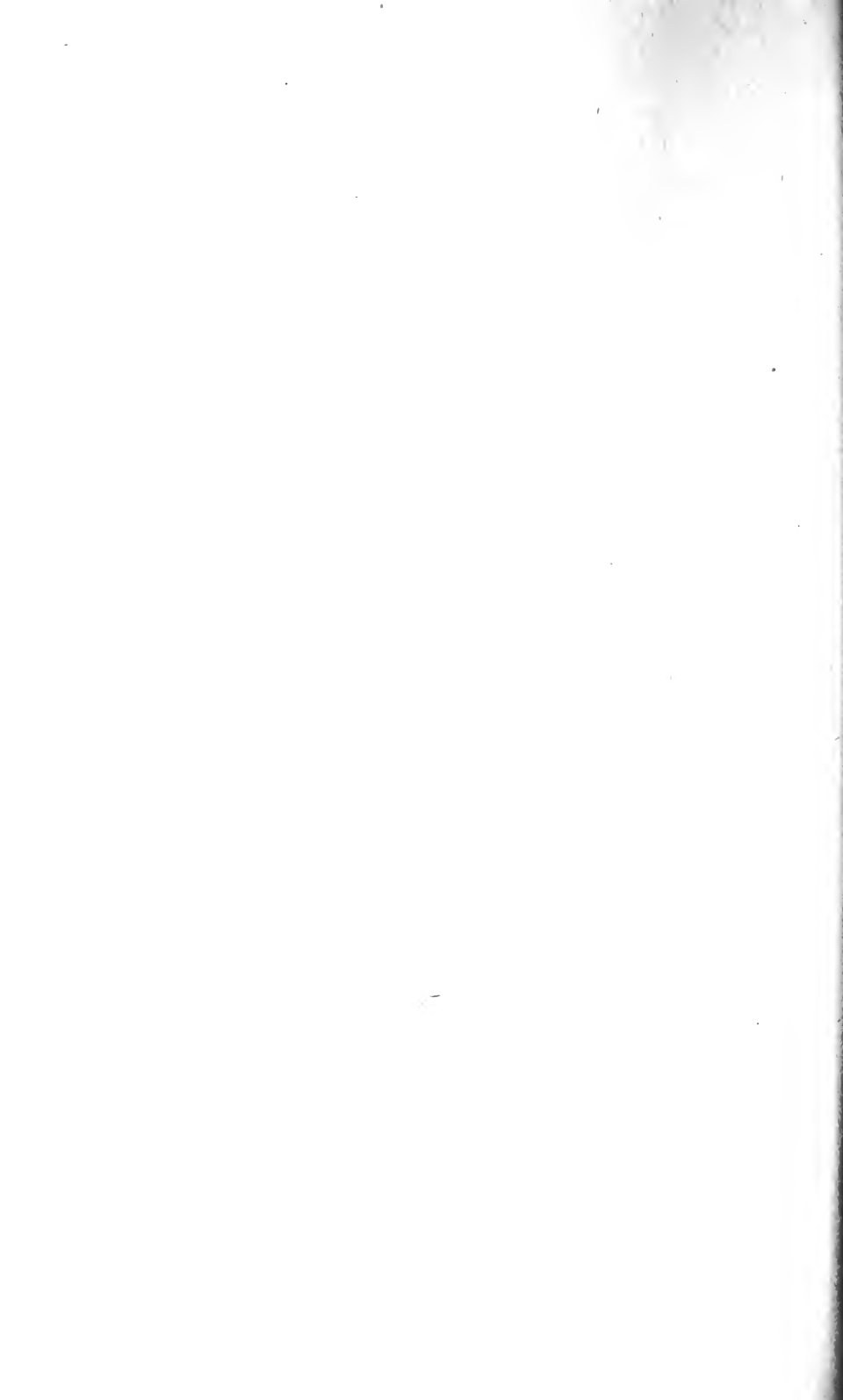
Conclusion.

The immigrant comes to the United States with long experience in a highly specialized field. The unions stand at the gate of employment and say “he shall not pass.” Since the depths of the depression, when unions were weak and disorganized, the unions have called upon the Government of the United States of America to give them help and aid in organizing the workmen throughout the nation, and they received powerful grants from their Government. The unions are strong. The immigrant is weak. The immigrant has asked the Federal Courts to adjudicate his claim that under the National Labor Relations Act, the Treaty with Poland, the United Nations Charter, and the Constitution of the United States, there reposes in him some legal right against this bar to his earning a living and becoming a worthy citizen of the United States.

Respectfully submitted,

HENRY B. ELY,

Attorney for Appellant.





APPENDIX "A."

CONSTITUTION OF THE UNITED STATES.

ARTICLE I.

Section 8.

"The Congress shall have Power * * *

"To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes;
* * *

ARTICLE VI.

"* * * and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; * * *"

FIFTH AMENDMENT.

"No person shall * * * be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

FOURTEENTH AMENDMENT.

"* * * nor shall any State deprive any person of life, liberty, or property, without due process of law; * * *"

APPENDIX "B."

NATIONAL LABOR RELATIONS ACT OF 1935.

Section 1 (29 U. S. C. A. 151):

" . . . The inequality of bargaining power between employees who do not possess full freedom of association or actual liberty of contract, and employers who are organized in the corporate or other forms of ownership association substantially burdens and affects the flow of commerce, and tends to aggravate recurrent business depressions, by depressing wage rates and the purchasing power of wage earners in industry and by preventing the stabilization of competitive wage rates and working conditions within and between industries.

Experience has proved that protection by law of the right of employees to organize and bargain collectively safeguards commerce from injury, impairment, or interruption, and promotes the flow of commerce by removing certain recognized sources of industrial strife and unrest, by encouraging practices fundamental to the friendly adjustment of industrial disputes arising out of differences as to wages, hours, or other working conditions, and by restoring equality of bargaining power between employers and employees.

It is declared to be the policy of the United States to eliminate the causes of certain substantial obstructions to the free flow of commerce and to mitigate and eliminate these obstructions when they have occurred by encouraging the practice and procedure of collective bargaining and by protecting the exercise by workers of full freedom of association, self-organization, and designation of representatives of their own choosing, for the purpose of negotiating the terms and conditions of their employment or other mutual aid or protection."

Section 2 (3) (29 U. S. C. A. 152):

“The term ‘employee’ shall include any employee, and shall not be limited to the employees of a particular employer, unless the chapter explicitly states otherwise, . . .”

Section 7 (29 U. S. C. A. 157):

“Employees shall have the right to self-organization, to form, join, or assist labor organizations, to bargain collectively through representatives of their own choosing, and to engage in concerted activities, for the purpose of collective bargaining or other mutual aid or protection.”

Section 8 (3) (29 U. S. C. A. 158):

“. . . *Provided*, That nothing in sections 151-166 of this title or in any other statute of the United States, shall preclude an employer from making an agreement with a labor organization (not established, maintained, or assisted by any action defined in sections 151-166 of this title as an unfair labor practice) to require as a condition of employment membership therein, if such labor organization is the representative of the employees as provided in section 159 (a) of this title, in the appropriate collective bargaining unit covered by such agreement when made.”

Section 9 (a) (29 U. S. C. A. 159):

“(a) Representatives designated or selected for the purposes of collective bargaining by the majority of the employees in a unit appropriate for such purposes, shall be the exclusive representatives of all the employees in such unit for the purposes of collective bargaining in respect to rates of pay, wages, hours of employment, or other conditions of employment: . . .”

APPENDIX "C."

TREATY BETWEEN THE UNITED STATES AND POLAND OF
FRIENDSHIP, COMMERCE, CONSULAR RIGHTS; PRO-
CLAIMED JULY 10, 1933; 48 STAT. L. 1507.

The United States of America and the Republic of Poland, desirous of strengthening the bond of peace which happily prevails between them, by arrangements designed to promote friendly intercourse between their respective territories through provisions responsive to the spiritual, cultural, economic and commercial aspirations of the peoples thereof, have resolved to conclude a Treaty of Friendship, Commerce and Consular Rights and for that purpose have appointed as their plenipotentiaries:

The President of the United States of America, Henry L. Stimson, Secretary of State of the United States of America, and

The President of the Republic of Poland, Tytus Filipowicz, Ambassador Extraordinary and Plenipotentiary of Poland in Washington,

Who, having communicated to each other their full powers found to be in due form, have agreed upon the following articles:

Article I. The nationals of each of the High Contracting Parties shall be permitted to enter, travel and reside in the territories of the other; to exercise liberty of conscience and freedom of worship; to engage in professional, scientific, religious, philanthropic, manufacturing and commercial work of every kind; to carry on every

form of commercial activity which is not forbidden by the local law; to own, erect, or lease and occupy appropriate buildings and to lease lands for residential, scientific, religious, philanthropic, manufacturing, commercial and mortuary purposes; to employ agents of their choice; and generally the said nationals shall be permitted, upon submitting themselves to all local laws and regulations duly established, to enjoy all of the foregoing privileges and to do anything incidental to or necessary for the enjoyment of those privileges, upon the same terms as nationals of the State of residence, except as otherwise provided by laws of either High Contracting Party in force at the time of the signature of this Treaty. In so far as the laws of either High Contracting Party in force at the time of the signature of this Treaty do not permit nationals of the other party to enjoy any of the foregoing privileges upon the same terms as the nationals of the State of residence, they shall enjoy, on condition of reciprocity, as favorable treatment as nationals of the most favored nation.

The nationals of either High Contracting Party within the territories of the other shall not be subjected to the payment of any internal charges or taxes other or higher than those that are exacted of and paid by its nationals.

The nationals of each High Contracting Party shall enjoy freedom of access to the courts of justice of the other on conforming to the local laws, as well for the prosecution as for the defense of their rights, in all degrees of jurisdiction established by law.

The nationals of each High Contracting Party shall receive within the territories of the other, upon submitting to conditions imposed upon its nationals, the most constant protection and security for their persons and property, and shall enjoy in this respect that degree of protection that is required by international law. Their property shall not be taken without due process of law and without payment of just compensation.

Nothing contained in this Treaty shall be construed to affect existing statutes of either of the High Contracting Parties in relation to emigration or to immigration or the right of either of the High Contracting Parties to enact such statutes, provided, however, that nothing in this paragraph shall prevent the nationals of either High Contracting Party from entering, traveling and residing in the territories of the other party in order to carry on international trade or to engage in any commercial activity related to or connected with the conduct of international trade on the same terms as nationals of the most favored nation.

Nothing contained in this Treaty is to be considered as interfering with the right of either party to enact or enforce statutes concerning the protection of national labor.

* * * * *

Article XII. The nationals of either High Contracting Party shall enjoy within the territories of the other, reciprocally and upon compliance with the conditions there imposed, such rights and privileges as have been or may hereafter be accorded the nationals of any other State

with respect to the organization of and participation in limited liability and other corporations and associations, for pecuniary profit or otherwise, including the rights of promotion, incorporation, purchase and ownership and sale of shares and the holding of executive or official positions therein. In the exercise of the foregoing rights and with respect to the regulation or procedure concerning the organization or conduct of such corporations or associations, such nationals shall be subjected to no conditions less favorable than those which have been or may hereafter be imposed upon the nationals of the most favored nation. The rights of any of such corporations or associations as may be organized or controlled or participated in by the nationals of either High Contracting Party within the territories of the other to exercise any of their functions therein, shall be governed by the laws and regulations, National, State or Provincial, which are in force or may hereafter be established within the territories of the party wherein they propose to engage in business.

APPENDIX "D."

CHARTER OF THE UNITED NATIONS.
59 Stat. L. 1046.

PREAMBLE.

We the peoples of the United Nations determined to save succeeding generations from the scourge of war, which twice in our lifetime has brought untold sorrow to mankind; and

to reaffirm faith in fundamental human rights, in the dignity and worth of the human person, in the equal rights of men and women and of nations large and small; and

to establish conditions under which justice and respect for the obligations arising from treaties and other sources of international law can be maintained; and

to promote social progress and better standards of life in larger freedom; and for these ends to practice tolerance and live together in peace with one another as good neighbors; and

to unite our strength to maintain international peace and security; and

to ensure, by the acceptance of principles and the institution of methods, that armed force shall not be used, save in the common interest; and

to employ international machinery for the promotion of the economic and social advancement of all peoples; have resolved to combined our efforts to accomplish these aims.

Accordingly, our respective Governments, through representatives assembled in the city of San Francisco, who have exhibited their full powers found to be in good and due form, have agreed to the present Charter of the United Nations and do hereby establish an international organization to be known as the United Nations.

CHAPTER I. PURPOSES AND PRINCIPLES.

Article 1.

The Purposes of the United Nations are:

1. To maintain international peace and security, and to that end: to take effective collective measures for the prevention and removal of threats to the peace, and for the suppression of acts of aggression or other breaches of the peace, and to bring about by peaceful means, and in conformity with the principles of justice and international law, adjustment or settlement of international disputes or situations which might lead to a breach of the peace;

2. To develop friendly relations among nations based on respect for the principle of equal rights and self-determination of peoples, and to take other appropriate measures to strengthen universal peace;

3. To achieve international cooperation in solving international problems of an economic, social, cultural, or humanitarian character, and in promoting and encouraging respect for human rights and for fundamental freedoms for all without distinction as to race, sex, language, or religion; and

4. To be a center for harmonizing the actions of nations in the attainment of these common ends.

Article 2.

The Organization and its Members, in pursuit of the purposes stated in Article 1, shall act in accordance with the following Principles:

1. The Organization is based on the principles of the sovereign equality of all its members.

2. All Members, in order to ensure to all of them the rights and benefits resulting from membership, shall fulfill in good faith the obligations assumed by them in accordance with the present Charter.

3. All Members shall settle their international disputes by peaceful means in such a manner that international peace and security, and justice are not endangered.

4. All Members shall refrain in their international relations from the threat or use of force against the territorial integrity or political independence of any state, or in any other manner inconsistent with the Purposes of the United Nations.

5. All Members shall give the United Nations every assistance in any action it takes in accordance with the present Charter, and shall refrain from giving assistance to any state against which the United Nations is taking preventive or enforcement action.

6. The Organization shall ensure that states which are not Members of the United Nations act in accordance with these Principles so far as may be necessary for the maintenance of international peace and security.

7. Nothing contained in the present Charter shall authorize the United Nations to intervene in matters which are essentially within the domestic jurisdiction of any state or shall require the Members to submit such matters to settlement under the present Charter; but this principle shall not prejudice the application of enforcement measures under Chapter VII.

Article 55.

With a view to the creation of conditions of stability and well-being which are necessary for peaceful and friendly relations among nations based on respect for the principle of equal rights and self-determination of peoples, the United Nations shall promote:

- a. Higher standards of living, full employment, and conditions of economic and social progress and development;
- b. Solutions of international economic, social, health, and related problems; and international cultural and educational cooperation; and
- c. Universal respect for, and observance of, human rights and fundamental freedoms for all without distinction as to race, sex, language, or religion.

Article 56.

All Members pledge themselves to take joint and separate action in cooperation with the Organization for the achievement of the purposes set forth in Article 55.

APPENDIX "E."

(OLD) 28 U. S. C. A. 41 (1):

"First. Of all suits of a civil nature, at common law or in equity, brought by the United States, or by any officer thereof authorized by law to sue, or between citizens of the same State claiming lands under grants from different States; or, where the matter in controversy exceeds, exclusive of interest and costs, the sum or value of \$3,000, and (a) arises under the Constitution or laws of the United States, or treaties made, or which shall be made, under their authority, . . ."

(NEW) 28 U. S. C. 1331:

"The district courts shall have original jurisdiction of all civil actions wherein the matter in controversy exceeds the sum or value of \$3,000, exclusive of interest and costs, and arises under the Constitution, laws or treaties of the United States."

(OLD) 28 U. S. C. A. 41 (8):

"Of all suits and proceedings arising under any law regulating commerce."

(NEW) 28 U. S. C. 1337:

"The district courts shall have original jurisdiction of any civil action or proceeding arising under any Act of Congress regulating commerce or protecting trade and commerce against restraints and monopolies."

(OLD) 28 U. S. C. A. 41 (12):

"Of all suits authorized by law to be brought by any person for the recovery of damages on account of any injury to his person or property, or of the deprivation of

any right or privilege of a citizen of the United States, by any act done in furtherance of any conspiracy mentioned in section 47 of Title 8.”

(OLD) 28 U. S. C. A. 41 (13):

“Of all suits authorized by law to be brought against any person who, having knowledge that any of the wrongs mentioned in section 47 of Title 8, are about to be done, and, having power to prevent or aid in preventing the same, neglects or refuses so to do, to recover damages for any such wrongful act.”

(OLD) 28 U. S. C. A. 41 (14):

“Of all suits at law or in equity authorized by law to be brought by any person to redress the deprivation, under color of any law, statute, ordinance, regulation, custom, or usage, of any State, of any right, privilege, or immunity, secured by the Constitution of the United States, or of any right secured by any law of the United States providing for equal rights of citizens of the United States, or of all persons within the jurisdiction of the United States.”

(NEW) 28 U. S. C. 1343:

“The district courts shall have original jurisdiction of any civil action authorized by law to be commenced by any person:

(1) To recover damages for injury to his person or property, or because of the deprivation of any right or privilege of a citizen of the United States, by any act done in furtherance of any conspiracy mentioned in section 47 of Title 8;

(2) To recover damages from any person who fails to prevent or to aid in preventing any wrongs mentioned in section 47 of Title 8 which he had knowledge were about to occur and power to prevent;

(3) To redress the deprivation, under color of any State law, statute, ordinance, regulation, custom or usage, of any right, privilege or immunity secured by the Constitution of the United States or by any Act of Congress providing for equal rights of citizens or of all persons within the jurisdiction of the United States.”

(OLD) 28 U. S. C. A. 41 (17):

“Of all suits brought by any alien for a tort only, in violation of the laws of nations or of a treaty of the United States.”

(NEW) 28 U. S. C. 1350:

“The district courts shall have original jurisdiction of any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States.”

(OLD) 28 U. S. C. A. 41 (23):

“Of all suits and proceedings arising under any law to protect trade and commerce against restraints and monopolies.”

(NEW) 28 U. S. C. 1337:

(See above).

APPENDIX "F."

SECTIONS OF U. S. C. A.

8 U. S. C. A. 41:

"All persons within the jurisdiction of the United States shall have the same right in every State and Territory to make and enforce contracts, to sue, be parties, give evidence, and to the full and equal benefit of all laws and proceedings for the security of persons and property as is enjoyed by white citizens, and shall be subject to like punishment, pains, penalties, taxes, licenses, and exactions of every kind, and to no other."

8 U. S. C. A. 43:

"Every person who, under color of any statute, ordinance, regulation, custom, or usage, of any State or Territory, subjects, or causes to be subjected, any citizen of the United States or other person within the jurisdiction thereof to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws, shall be liable to the party injured in any action at law, suit in equity, or other proper proceeding for redress."

8 U. S. C. A. 47 (3):

"If two or more persons in any State or Territory conspire or go in disguise on the highway or on the premises of another, for the purpose of depriving, either directly or indirectly, any person or class of persons of the equal protection of the laws, or of equal privileges and immunities under the laws; * * * in any case of conspiracy set forth in this section, if one or more persons engaged therein do, or cause to be done, any act in furtherance of the object of such conspiracy, whereby another is injured in his person or property, or deprived of having and exercising any right or privilege of a citizen of the United States, the party so injured or deprived may have an action for the recovery of damages, occasioned by such injury or deprivation, against any one or more of the conspirators."

APPENDIX "G."

SECTIONS OF LABOR CODE, STATE OF CALIFORNIA.

§921. *Promise as to joining, remaining in, or withdrawing from labor organizations. Relief:*

[Promises contrary to public policy.] Every promise made after August 21, 1933, between any employee or prospective employee and his employer, prospective employer or any other person is contrary to public policy if either party thereto promises any of the following:

(a) To join or to remain a member of a labor organization or to join or remain a member of an employer organization,

(b) Not to join or not to remain a member of a labor organization or of an employer organization.

(c) To withdraw from an employment relation in the event that he joins or remains a member of a labor organization or of an employer organization.

[Promise no basis for relief.] Such promise shall not afford any basis for the granting of legal or equitable relief by any court against a party to such promise, or against any other persons who advise, urge, or induce, without fraud or violence or threat thereof, either party thereto to act in disregard of such promise.

§922. *Coercing agreement not to join labor organization. Misdemeanor:*

Any person or agent or officer thereof who coerces or compels any person to enter into an agreement, written or verbal, not to join or become a member of any labor organization, as a condition of securing employment or continuing in the employment of any such person is guilty of a misdemeanor.

§923. *Public policy as to labor organizations.*

In the interpretation and application of this chapter, the public policy of this State is declared as follows:

Negotiation of terms and conditions of labor should result from voluntary agreement between employer and employees. Governmental authority has permitted and encouraged employers to organize in the corporate and other forms of capital control. In dealing with such employers, the individual unorganized worker is helpless to exercise actual liberty of contract and to protect his freedom of labor, and thereby to obtain acceptable terms and conditions of employment. Therefore it is necessary that the individual workman have full freedom of association, self-organization, and designation of representatives of his own choosing, to negotiate the terms and conditions of his employment, and that he shall be free from the interference, restraint, or coercion of employers of labor, or their agents, in the designation of such representatives or in self-organization or in other concerted activities for the purpose of collective bargaining or other mutual aid or protection.

APPENDIX "H."

SECTION OF LABOR MANAGEMENT RELATIONS ACT, 1947.

Section 301 (c):

For the purposes of actions and proceedings by or against labor organizations in the district courts of the United States, district courts shall be deemed to have jurisdiction of a labor organization (1) in the district in which such organization maintains its principal office, or (2) in any district in which its duly authorized officers or agents are engaged in representing or acting for employee members.

APPENDIX "I."

15 U. S. C. A. 15.

Any person who shall be injured in his business or property by reason of anything forbidden in the anti-trust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover three-fold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee. Oct. 15, 1914, c. 323 §4, 38 Stat. 731.

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Answering Brief of Appellees International Photogra-
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Appellees.

Answering Brief of Appellees International Photographers of the Motion Picture Industry Local 659, Etc., and Herbert Aller.

Additional Statement of the Case.

Appellee International Photographers of the Motion Picture Industry Local 659, etc., hereinafter referred to as Defendant Local, is a labor organization whose members, including first cameramen, are employed in the Hollywood motion picture studios; appellee Aller is its business representative; appellant, appellee Aller, and all members of Defendant Local are residents and citizens of the State of California. *Diversity of citizenship is not asserted; its absence affirmatively appears.*

Appellant seeks to recover damages for past and prospective loss of earnings, humiliation, worry, frustration, and loss of prestige, all resulting, he claims, from the refusal of Defendant Local to admit him into membership. Defendant Local, for several years last past, has had, and now has, a closed-shop contract with the Hollywood

Studios, expiring, according to the complaint, on December 31, 1948. The District Court granted motions interposed by the appellees to dismiss and entered a judgment of dismissal for lack of jurisdiction [28-29*].

In Paragraph XI of his complaint [11], appellant alleges that ever since January 1, 1942, Defendant Local has refused to admit him to membership and, with the exceptions thereafter noted, has refused to permit him to work as a first cameraman for any employer engaged in the production of motion pictures within the State of California. He alleges in Paragraph XVI of the complaint [13] that ever since January 1, 1942, the Constitution of appellee International Alliance, etc., the parent organization of Defendant Local, has provided that "no person shall be eligible to membership in said Alliance who is not a citizen of the United States or Canada, or of any other territory in which The Alliance exercises jurisdiction," and that Defendant Local and its members consider said constitutional provision to be binding upon them and have, ever since January 1, 1942, until July 11, 1947, when appellant became a citizen of the United States, treated such constitutional provision as one of the grounds for refusing to admit appellant to membership. It is further alleged in Paragraph XVII [13] that Defendant Local and its members have never advised appellant of any reason for the denial of membership, except that same was "contrary to their Constitution or that employment as first cameraman was desired for the members of" Defendant Local.

In Paragraph XIX of his complaint [14] appellant alleges that the defendant "permitted" him to be employed

*Figures appearing in brackets refer, unless otherwise noted, to pages of Transcript of Record.

on three productions of motion pictures, one *in 1945*, another *in 1946*, and another *in 1947*, under certain terms and conditions laid down by Defendant Local.

With respect to the closed-shop contracts existing between Defendant Local and the Hollywood Studios, appellant alleges in Paragraph VII of his complaint [7-8] as follows:

“Local 659 is a labor organization having as one of its purposes the collective bargaining with employers upon negotiation of wages, hours and working conditions for its members; that officers and agents of Local 659 are engaged in representing and act for employee members within the above entitled district, and Local 659 maintains its principal office therein; on December 10, 1942, and all times thereafter Local 659 was a chartered local union of the IATSE; ever since December 10, 1942, Local 659 has been designated by a majority of first cameramen in said State of California as their exclusive bargaining agency on wages, hours and working conditions and, ever since the said date, Local 659 has represented first cameramen in negotiations with all employers engaged in the production of motion pictures within said State as aforesaid; *that Local 659 is not established, maintained or dominated by any employer*; ever since December 10, 1942, there has been no controversy between any employer and Local 659 as to whether or not Local 659 was the exclusive bargaining agency for first cameramen on wages, hours and working conditions of first cameramen; at all times since that date Local 659 has acted as the exclusive bargaining agency on wages, hours and working conditions of first cameramen; pursuant to, by virtue of and under the color of the authority granted to it by the National Labor Relations Act, Sections 921-923 of the

Labor Code of the State of California, and the law of the State of California, Local 659, *on or about January 1, 1943*, entered into contracts with all employers engaged in the production of motion pictures as aforesaid within the State of California, requiring as a condition of employment that all first cameramen be and remain members in good standing of Local 659, a contract with such provision being commonly known as a closed shop contract; closed shop contracts for first cameramen between Local 659 and all employers engaged in the motion picture industry within said State have remained in full force and effect from *on or about January 1, 1943*, to and including the date of the filing of this complaint; the last agreement entered into by and between IATSE, Local 659, and all employers engaged in the production of motion pictures in said State was executed in writing *as of January 1, 1946*, for a term *ending December 31, 1948*, and provides that Local 659 shall represent all first cameramen for the purpose of collective bargaining and that employers engaged in the production of motion pictures will employ only first cameramen who are members in good standing of Local 659, and that Local 659 will furnish competent men to perform the work and render the services required by the employer of first cameramen."

It will be observed from the foregoing that appellant was not employed as a first cameraman, or in any other capacity, by any of the Hollywood Studios with which Defendant Local has or has had closed-shop contracts *at the time such closed-shop contracts were executed*. So far as the particular work which appellant was "permitted" by Defendant Local to do *in 1945, in 1946, and in 1947*, it is obvious that these three assignments were executed by appellant as a permittee of Defendant Local.

I.

The Rights, Privileges, and Immunities Granted Aliens by Treaties to Which the United States Is a High Contracting Party Will Be Protected by the United States Courts Only Against Action by States or Political Divisions Thereof; in the Instant Action, Appellant Is Not Deprived of Any Right by Any Action of the State of California or Its Political Subdivisions.

For the purpose of our discussion on this point, we will assume *arguendo* that the Treaty with Poland and the Charter of the United Nations each contains a provision specifically providing that citizens of Poland residing in the United States shall have the right to work as first cameramen in motion picture studios located in the State of California. Such construction of these treaties, however, will avail appellant nothing and does not vest jurisdiction in the District Court in the instant action. Treaties to which the United States is a party, it is true, are part of the supreme law of the land, but only when official action by a state or a political subdivision thereof, by enactment of state legislation or city ordinance, deprives an alien of a right, privilege, or immunity protected and guaranteed by such treaty, do the federal courts acquire jurisdiction. As said by the Supreme Court of the United States in *Asakura v. Seattle*, 265 U. S. 332-341, 68 L. Ed. 1041-1044:

“Treaties for the protection of citizens of one country residing in the territory of another are numerous, and make for good understanding between nations. * * * The rule of equality established by it cannot be rendered nugatory in any part of the United States *by municipal ordinances or state laws.*”*

*Italics appearing in this brief are ours unless otherwise indicated.

The rights given by treaties are not protected against individual action any more than the rights guaranteed by the Fifth and the Fourteenth Amendments to the Constitution are protected against individual action. (Point VI, *infra*.)

The quotations from the opinions of Mr. Justice Black and Mr. Justice Murphy in *Oyama v. State of California*, 332 U. S. 633, 68 S. Ct. 269 at 277 and 278, appearing on page 33 of appellant's opening brief, in no manner sustain appellant's contention that the District Court has jurisdiction of the instant action under the United Nations Charter. The question before the Supreme Court in the *Oyama* case, *supra*, was whether a statute of the State of California unconstitutionally abridged the rights of a Japanese alien. That Mr. Justice Black in referring, as he did, to the Charter of the United Nations had in mind State action, as distinguished from action of private individuals, is clearly evidenced by his use of the words "if state laws," appearing in the last sentence of the quotation from his opinion set forth in appellant's brief and reading as follows:

"How can this nation be faithful to this international pledge if *state laws* which bar land ownership and occupancy by aliens on account of race are permitted to be enforced?"

The use of the word "statute" in the concluding sentence of the quotation from Mr. Justice Murphy's opinion is likewise significant, such sentence reading as follows:

"Its" (referring to the Alien Land Law) "inconsistency with the Charter, which has been duly ratified and adopted by the United States, is but one more reason why the *statute* must be condemned."

II.

A Case Does Not Arise “Under the Constitution or Laws of the United States” Unless It Involves a Real and Substantial Dispute Respecting the Validity, Construction, or Effect of the Constitution or Such Laws, Upon the Determination of Which the Result Depends.

AUTHORITIES:

Shulthis v. McDougal, 225 U. S. 561, 569, 56 L. Ed. 1205, 1211;

Gully v. First National Bank, 299 U. S. 109, 112, 81 L. Ed. 70, 72;

Schatte, et al. v. International Alliance, etc., et al., 70 Fed. Supp. 1008; affirmed 165 F. 2d 216 (9th C. C. A.), cert. denied May 3, 1947, 68 S. Ct. 1018, 92 L. Ed. 985.

In *Shulthis v. McDougal*, 225 U. S. 561, 569, 56 L. Ed. 1205, 1211, the Supreme Court said:

“A suit to enforce a right which takes its origin in the laws of the United States is not necessarily, or for that reason alone, one arising under those laws, for a suit does not so arise unless it really and substantially involves a dispute or controversy respecting the validity, construction or effect of such a law, upon the determination of which the result depends.”

And in *Gully v. First National Bank*, 299 U. S. 109, 112, 81 L. Ed. 70, 72, the same court used this language:

“How and when a case arises ‘under the Constitution or laws of the United States’ has been much considered in the books. Some tests are well established. To bring a case within the statute, a right or immunity created by the Constitution or laws of the

United States must be an element, and an essential one, of the plaintiff's cause of action. (Citing cases.) *The right or immunity must be such that it will be supported if the Constitution or laws of the United States are given one construction or effect, and defeated if they receive another."*

Schatte, et al. v. International Alliance, supra, which is the latest authority on the subject, states the rules as follows:

"From the mere fact that a right was established by federal law, it does not follow that all litigation growing therefrom arises under the laws of the United States. Actions growing from the issue of federal land grants do not arise 'under the laws of the United States.' *Shoshone Mining Co. v. Rutter*, 177 U. S. 505, 20 S. Ct. 726, 44 L. Ed. 864; *Shulthis v. McDougal*, 225 U. S. 561, 569, 32 S. Ct. 704, 707, 56 L. Ed. 1205; *Marshall v. Desert Properties*, 9 Cir., 103 F. 2d 551, certiorari denied 308 U. S. 563, 60 S. Ct. 74, 84 L. Ed. 473. An action brought to enforce a right under a contract which is made as the result of rights granted under the patent laws to receive royalties upon sale or license of the patented device is not an action arising under the laws of the United States. *Odell v. Farnsworth*, 250 U. S. 501, 504, 39 S. Ct. 516, 63 L. Ed. 1111. To come within the provisions of these sections, the suit must really and substantially involve a dispute respecting the validity, construction, or effect of some law of the United States, upon the determination of which the result depends. *Malone v. Gardner*, 4 Cir., 62 F. 2d 15; *Delaware, Lackawanna & Western R. v. Slocum*, D. C., 56 F. Supp. 634."

III.

**District Court Had No Jurisdiction Herein by Virtue
of Any of the Provisions of the Anti-Trust Laws.**

AUTHORITIES:

U. S. C. A., Section 41(23), Title 28;

U. S. C. A., Section 15, Title 15;

U. S. C. A., Section 17, Title 15;

Allen Bradley Co. v. Local Union No. 3, 325 U. S. 797, 89 L. Ed. 1939;

Hunt v. Crumboch, 325 U. S. 821, 89 L. Ed. 1954;

United States v. Hutcheson, 312 U. S. 219, 85 L. Ed. 788.

Section 41(23), Title 28, U. S. C. A., grants jurisdiction to the District Courts "of all suits and proceedings arising under any law to protect trade and commerce against restraints and monopolies," and Section 15, Title 15, provides that "any person who shall be injured in his business or property by reason of anything forbidden in the anti-trust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee." The foregoing are among the statutes of the United States which appellant claims vest jurisdiction in this Court over the instant action; we submit that there is nothing in the complaint which even remotely suggests that the cause of action sought to be described therein comes within the provisions of the Anti-Trust Laws. Section 17, Title 15, U. S. C. A., which is part of the federal statutes relating to monopolies and

combinations, specifically excludes labor organizations from the terms of the Anti-Trust Laws. It reads as follows:

“The labor of a human being is not a commodity or article of commerce. *Nothing contained in the anti-trust laws shall be construed to forbid the existence and operation of labor, agricultural, or horticultural organizations, instituted for the purposes of mutual help, and not having capital stock or conducted for profit, or to forbid or restrain individual members of such organizations from lawfully carrying out the legitimate objects thereof; nor shall such organizations, or the members thereof, be held or construed to be illegal combinations or conspiracies in restraint of trade, under the anti-trust laws.*”

The Supreme Court of the United States has on numerous occasions held that, irrespective of the effect of its action upon interstate commerce, a labor union acting alone, and not in combination with business men, does not violate the Sherman Anti-Trust Act; there are no allegations in the complaint herein which even hint at any combination between Defendant Local and employers to restrain competition in, or to monopolize the marketing of, or fix prices of, any product of such employers moving in interstate commerce. The facts set forth in the complaint in the instant case bear no resemblance to the situation which was before the Supreme Court of the United States in *Allen Bradley Co. v. Local Union No. 3*, 325 U. S. 797, 89 L. Ed. 1939. That the closed-shop contract possessed by Defendant Local, the operation of which precludes plaintiff from obtaining employment as a first cameraman with the employers with whom Defendant Local has such closed-shop contract, is a legitimate objec-

tive of organized labor, that is to say, that closed-shop contracts are valid and enforceable, is such an elementary proposition that no citation of authority in support thereof is necessary. Not only is Defendant Local specifically excluded from the provisions of the Sherman Anti-Trust Laws by reason of the express terms of Section 17, Title 15, U. S. C. A., above quoted, but the rule of law enunciated by the Supreme Court of the United States in *Hunt v. Crumboch*, 325 U. S. 821, 89 L. Ed. 1954; *United State v. Hutcheson*, 312 U. S. 219, 85 L. Ed. 788, and other cases, is controlling. It is only when labor organizations aid and combine with non-labor groups to create business monopolies and to control the marketing of goods that the provisions of the Sherman Anti-Trust Law become applicable. As said by our Supreme Court in the *Hutcheson* case, 312 U. S. at 232, 85 L. Ed. at 793:

“So long as a union acts in its self-interest and does not combine with non-labor groups, the licit and the illicit under Section 20 are not to be distinguished by any judgment regarding the wisdom or unwisdom, the rightness or wrongness, the selfishness or unselfishness of the end of which the particular union activities are the means.”

And as said by the Supreme Court of the United States in *Hunt v. Crumboch*, 89 L. Ed. 1956, 325 U. S. at 825:

“A worker is privileged under congressional enactments, acting either alone or in concert with his fellow workers, to associate or to decline to associate with other workers, to accept, refuse to accept, or to terminate a relationship of employment, and his labor is not to be treated as ‘a commodity or article of commerce.’ Clayton Act, 38 Stat. 730, 731, c. 323; Norris-Laguardia Act (March 23, 1932), 47 Stat.

70, 90, 29 USCA, Section 101, 9 FCA title 29, Section 101. See also *American Foundries v. Tri-City Central Trades Council*, 257 US 184, 209, 66 L. Ed. 189, 199, 42 S. Ct. 72, 27 ALR 360.”

Concedely it is the law in California and in some other jurisdictions that, while a closed shop of itself is lawful and an *arbitrarily* closed union of itself is lawful, the synchronization of both is condemned as a “monopoly.” This doctrine was first enunciated in the *James* case (25 Cal. 2d 721), and has been followed in companion cases thereto. The relief which has been granted in the California Courts to a person unable to obtain employment at a particular job, by reason of the existence of a close-shop contract and the *arbitrary* refusal of the labor organization possessing such closed-shop contract to admit such person into membership, consists in directing such labor organization to admit such person into membership *or* be restrained from enforcing the closed shop against him. The relief has always been granted in the alternative; the labor organization has its choice between admission of the applicant to membership or permitting him to work without *indicia* of membership. It must be emphasized, however, that even under the *James* case doctrine rejection of membership must be *arbitrary*, and if an applicant cannot meet reasonable requirements, terms, and conditions applicable to all, his rejection for that reason is not considered *arbitrary*. As was said in the *Williams* case (27 Cal. 2d 586 at 591), companion case to the *James* case:

“The individual worker denied the right to *keep his job* suffers a loss, and his right to protection

against such arbitrary and discriminatory exclusion from union membership should be recognized wherever membership is a necessary prerequisite to work."

and the Court protected such "right" by restraining the labor organization from enforcing its closed-shop contract against the plaintiff in the particular case. Furthermore, the Supreme Court of California in the *James* case recognized "the right of the union to *reject* or expel persons who refuse to abide by any reasonable regulation of lawful policy adopted by the union." (25 Cal. 2d at 736.)

In the *James* and companion cases, the plaintiffs therein were Negroes; the defendant labor organization holding the closed-shop contract, by its constitution, specifically excluded Negroes from membership. The discrimination, therefore, was one based solely upon skin pigmentation. The same situation existed in the *Corsi* case (326 U. S. 88, 89 L. Ed. 2072), cited by appellant in his brief herein. That situation does not exist in the instant case. We deny, but will assume *arguendo*, that under the doctrine of the *James* case Defendant Local has a "monopoly," as that word is used in the State Court decision, in view of the synchronization of its closed shop and alleged closed union. *Nevertheless, such fact in no manner gives this Court jurisdiction of the instant controversy.* The monopoly contemplated by the federal anti-trust laws is not such a "monopoly" as that described in the *James* and companion cases, *i. e.*, "of the supply of labor." Furthermore by the express terms of the federal anti-trust laws labor organizations are excluded from their operation.

IV.

**Statutes of the United States "Regulating Commerce"
Do Not Vest Jurisdiction in the District Court
Over the Instant Action.**

AUTHORITIES:

U. S. C. A., Section 41(8), Title 28;

Delaware L. & W. R. Co. v. Slocum, 56 Fed. Supp.
634;

Schatte, et al. v. International Alliance, etc., et al.,
70 Fed. Supp. 1008, Affirmed 165 F. 2d 216
(C. C. A. 9th), cert. denied May 3, 1947, 68 S.
Ct., 1018, 92 L. Ed. 985.

Appellant asserts that the District Court has jurisdiction by reason of Section 41(8), Title 28, U. S. C. A., which grants jurisdiction to the United States District Courts "of all suits and proceedings arising under any law regulating commerce"; we submit that this statute has no application herein. The controversy presented by appellant's complaint does not arise out of any law *regulating commerce*; the fact that a controversy may *affect* interstate commerce does not give District Courts of the United States jurisdiction of such controversies.

In *Delaware L. & W. R. Co. v. Slocum*, 56 Fed. Supp. 634, the District Court for the Western District of New York had before it an action filed by an employer against competing labor unions in which declaratory relief was sought, the employer desiring a judgment construing certain separate contracts between the employer and two

labor organizations. Each of the labor organizations claimed jurisdiction over and the right to represent “crew callers” and insisted that under their respective contracts with the employer each had jurisdiction over such classification of work. Motions to dismiss were interposed upon the ground that the Court lacked jurisdiction. We quote from the opinion as follows:

“A suit does not arise under the laws of the United States unless it ‘really and substantially involves a dispute or controversy respecting the validity, construction, or effect of some law of the United States, upon the determination of which the result depends.’ (Citing cases.) It is patent from the complaint that this suit does not involve the ‘validity, construction, or effect’ of any federal statute, but rather seeks the determination of its rights or liabilities under certain contracts. It has been urged that this is a suit for a violation of the commerce laws, 28 U. S. C. A., Sec. 41(8), and that this court has original jurisdiction. The nature of the suit is to be determined by the complaint (citing cases) and nothing therein reveals that the acts charged have any relation to the commerce laws. It is true that the plaintiff in the operation of its railroad was engaged in interstate commerce, *but the mere fact that interstate commerce may be affected is not sufficient to give jurisdiction in a private suit unless the suit directly concerns an Act of Congress.* (Citing cases.)”

To the same effect is *Schatte, et al. v. International Alliance, supra*:

“28 U. S. C. A., Sec. 41(8) confers jurisdiction on the District Courts of the United States in ‘all suits and proceedings arising under any law regulating commerce,’ without regard to the jurisdictional amount requirement of 28 U. S. C. A., Sec. 41(1). Since more than \$3,000 is involved in this action, Section 41(8) will not establish jurisdiction in this court if it cannot be established under Section 41(1), which grants jurisdiction in all suits where the matter in controversy exceeds \$3,000 and ‘arises under the Constitution or laws of the United States.’

“It is not enough that the dispute should merely *affect* commerce to bring it within the scope of Section 41(8) or Section 41(1). *Delaware, Lackawanna & Western R. v. Slocum*, D. C., 56 Fed. Supp. 634.

“In *Gully v. First National Bank*, 299 U. S. 109, at page 112, 57 S. Ct. 96, at page 97, 81 L. Ed. 70, Mr. Justice Cardozo said:

“‘To bring a case within the statute, a right or immunity created by the Constitution or laws of the United States must be an element, and an essential one, of the plaintiff’s cause of action. * * * The right or immunity must be such that it will be supported if the Constitution or laws of the United States are given one construction or effect, and defeated if they receive another.’”

V.

**Neither National Labor Relations Act Nor Labor-
Management Relations Act, 1947, Vests Jurisdic-
tion in the District Court Over Subject Matter of
Action or Parties Thereto.**

AUTHORITIES:

- N. L. R. A.*, 29 U. S. C. A., Sections 151-166;
L. M. R. A., 1947, 29 U. S. C. A., Sections 141-
197;
*Donnelly Garment Co. v. International Ladies'
Garment Workers' Union*, 99 F. 2d 309 at 315;
Fur Workers Union, etc. v. Fur Workers Union,
105 F. 2d 1 at 12 (affirmed in 308 U. S. 522,
84 L. Ed. 443);
N. L. R. A., Section 10(e), (1);
L. M. R. A., 1947, Section 301(a);
L. M. R. A., 1947, Section 303;
L. M. R. A., 1947, Section 102;
L. M. R. A., 1947, Section 8(3);
Amazon Mills Co. v. Textile Workers Union (C.
C. A. 4, 1948), 167 F. 2d 183;
Gerry of California v. Superior Court (1948), 32
A. C. 141, 194 P. 2d 689.

Among the statutes of the United States asserted by appellant as vesting jurisdiction in the District Court are the National Labor Relations Act (*N. L. R. A.*) (29 U. S. C. A., Sections 151-166) enacted July 5, 1935, and its successor, the Labor-Management Relations Act, 1947, (*L. M. R. A.*) (29 U. S. C. A., Sections 141-197) enacted

June 23, 1947, with certain provisions respecting closed shops not operative until August 22, 1947. Under N. L. R. A. no jurisdiction of any sort was vested in the District Courts of the United States; the National Labor Relations Board was given exclusive power to enforce rights guaranteed by that Act to employees, subject only to review by the proper Circuit Courts of Appeals. Thus, Section 10(a) of the N. L. R. A. (29 U. S. C. A., 160(a)), reads as follows:

“The Board is empowered, as hereinafter provided, to prevent any person from engaging in any unfair labor practice (listed in section 158) affecting commerce. This power shall be exclusive, and shall not be affected by any other means of adjustment or prevention that has been or may be established by agreement, code, law, or otherwise.”

Judge Sanborn, speaking for the Circuit Court of Appeals, Eight Circuit, in *Donnelly Garment Co. v. International Ladies' Garment Workers' Union*, 99 F. 2d 309 at 315, said:

“It also seems clear to us that the *only* jurisdiction conferred by the National Labor Relations Act upon federal courts is that conferred upon the Circuit Courts of Appeals with respect to enforcing, modifying and setting aside orders of the National Labor Relations Board.”

The relative jurisdictions of the Federal Courts and the National Labor Relations Board under the provisions of N. L. R. A. are expressed clearly and at length by the

United States Court of Appeals for the District of Columbia in *Fur Workers Union, etc. v. Fur Workers Union*, 105 F. 2d 1 at 12 (affirmed in 308 U. S. 522, 84 L. Ed. 443).

Other decisions exist and might be cited in support of our contention that District Courts of the United States under N. L. R. A. had no jurisdiction of actions such as that set forth in the complaint herein, or, for that matter, any other action purportedly arising under N. L. R. A. However, in view of the fact that the rule above set forth is so clearly and uniformly established, without dissent or suggestion thereof, we deem it unnecessary to cite further authorities.

It is true that when Congress enacted L. M. R. A., 1947, it vested in District Courts of the United States jurisdiction over certain actions, which jurisdiction had not previously been vested in such Courts pursuant to N. L. R. A. By the terms of Section 10(e), (1), the National Labor Relations Board in its own name may institute actions in the appropriate District Courts to restrain certain specifically defined unfair labor practices. Obviously, the complaint in the instant case does not come within the purview of such Section; jurisdiction thereby is vested only in actions brought by the N. L. R. B. and for the purpose of preventing certain unfair labor practices.

Another section of L. M. R. A., 1947, vesting jurisdiction in the District Courts, where such jurisdiction did not previously exist, is Section 301(a), which reads as follows:

“Suits for violation of contracts between an employer and a labor organization representing employees in an industry affecting commerce as defined in this Act, or between any such labor organizations,

may be brought in any district court of the United States having jurisdiction of the parties, without respect to the amount in controversy or without regard to the citizenship of the parties.”

The instant case does not come within the foregoing and above quoted section because (a) it is not a suit for violation of a contract between an employer and a labor organization, etc., and (b) said section does not contemplate an action brought by an individual, but was intended by Congress to grant jurisdiction to the United States District Courts in actions between employers and labor organizations based upon alleged violations of collective bargaining agreements.

Section 303, L. M. R. A., 1947, makes unlawful, for the purposes of that section only, secondary boycotts, unfair labor practices, and jurisdictional strikes, and then provides in subsection (b) thereof as follows:

“Whoever shall be injured in his business or property by reason of any violation of subsection (a) may sue therefor in any district court of the United States subject to the limitations and provisions of section 301 hereof without respect to the amount in controversy, or in any other court having jurisdiction of the parties, and shall recover the damages by him sustained and the cost of the suit.”

Since the complaint herein does not in any manner relate to secondary boycotts, unfair labor practices, or jurisdictional strikes, the subject matter thereof does not come within the provisions of Section 303 above quoted. (Fur-

thermore, while Section 301 specifically waives amount in controversy and diversity of citizenship, Section 303 waives only amount in controversy; thus, in any event, in an action brought under Section 303 diversity of citizenship is a requisite.

District Courts of the United States are likewise given jurisdiction with respect to the criminal provision defined in Section 302, L. M. R. A., 1947, relating to restrictions on payments to employee representatives, but, of course appellant makes no claim that pursuant to that section the District Court has jurisdiction over the instant action. So far as we are advised, the foregoing constitute the only provisions of L. M. R. A., 1947, vesting jurisdiction in District Courts of the United States, and such jurisdiction in those instances is expressly limited as to parties and subject matter; neither appellant nor the subject matter of his action comes within the purview of such permitted actions or vested jurisdiction. Furthermore, under Section 102, L. M. R. A., 1947, any closed-shop contract existing on June 23, 1947, when that Act was enacted, is recognized as being valid and enforceable to the date of its expiration, and any closed-shop contract executed prior to August 22, 1947, and after June 22nd, 1947, is likewise so recognized, provided it is not for a period of more than one year. The complaint in the instant case (Paragraph VII (8)) sets forth the fact that Defendant Local has a closed-shop contract ending December 31, 1948, which was executed on January 1, 1946. Hence, under the terms of said Section 102, L. M. R. A., 1947, the closed-shop

contract of Defendant Local is valid, enforceable, and not against public policy. Upon the expiration of the closed-shop contract held by Defendant Local appellant has the right, pursuant to Section 8(3) of L. M. R. A., 1947, to obtain employment as a first cameraman, if such he can obtain, without being a member of Defendant Local, and within thirty days after obtaining such employment must apply for membership in Defendant Local provided, in accordance with said section of that Act, Defendant Local then has a Union Shop, and if Defendant Local does not accept him into membership in accordance with said section it cannot exercise its economic strength or in any manner bring about appellant's discharge by his employer.

If the acts of the appellees of which appellant complains constitute violations of the Labor-Management Relations Act, 1947, no District Court has jurisdiction over same as such jurisdiction is by said Act vested exclusively in the National Labor Relations Board. (*Amazon Mills Co. v. Textile Workers Union, supra*; *Gerry of California v. Superior Court, supra*.)

VI.

Jurisdiction Is Not Vested in the District Court Over the Instant Action Under the Fifth or the Fourteenth Amendments to the Constitution of the United States, Nor by Secion 41, Title 28, USCA, or Any Subsection Thereof, Section 43, Title 8, USCA, Section 47(3), Title 8, USCA, Section 48, Title 8, USCA, Nor by Civil Rights Statutes.

AUTHORITIES:

Corrigan v. Buckley, 271 U. S. 323, 330, 70 L. Ed. 969, 972;

Civil Rights Cases, 109 U. S. 3, 27 L. Ed. 836;

Virginia v. Rives, 100 U. S. 313, 25 L. Ed. 667;

United States v. Harris, 106 U. S. 629, 639, 27 L. Ed. 290, 294;

California Oil and Gas Co. v. Miller, 96 Fed. 12, 22;

Love v. Chandler, 124 F. 2d 785 (C. C. A. 8);

Simpson v. Geary, 204 Fed. 507;

Mitchell v. Greenough (C. C. A. 9), 100 F. 2d 184, 187; cert. denied 306 U. S. 659, 83 L. Ed. 1056;

Love v. United States, 108 F. 2d 43, 45-46 (cert. denied 309 U. S. 673, 84 L. Ed. 1018);

Brents v. Stone, et al., 60 Fed. Supp. 82;

Emmons v. Smitt, et al., 58 Fed. Supp. 869;

Haywood v. United States, 268 Fed. 795;

United States v. Moore, 129 Fed. 630;

Schatte, et al. v. International Alliance, etc., et al., 70 Fed. Supp. 1008; affirmed 165 F. 2d 216 (9th C. C. A.); cert. denied 92 L. Ed. 985.

The Constitutional Amendments and Statutes of the United States referred in the above point are relied upon by appellant in support of his contention that the District Court has jurisdiction of the subject matter of and parties to this action. They all relate to the powers, privileges, and immunities granted citizens of and persons residing in the United States. In our opinion, the cause of action which appellant seeks to allege in his complaint is not one arising out of, secured by, nor dependent upon any of the Constitutional Amendments or Statutes which we have grouped for discussion under this point.

It has long been settled that the Fifth Amendment to the Constitution of the United States is a limitation only upon the federal government and does not limit individual action. In the language of *Corrigan v. Buckley*, 271 U. S. 323, 330, 70 L. Ed. 969, 972:

“The 5th Amendment ‘is a limitation only upon the powers of the general government,’ *Talton v. Mayes*, 163 U. S. 376, 382, 41 L. Ed. 196, 198, 16 Sup. Ct. Rep. 986, and is not directed against the action of individuals.”

In the *Civil Rights Cases*, 109 U. S. 3, 27 L. Ed. 836, the Supreme Court of the United States, years ago, interpreted the Fourteenth Amendment to the Constitution of the United States as applying solely to state action and not to individual action. In the language of that Court in that decision:

“It is state action of a particular character that is prohibited. Therefore, invasion of individual rights is not the subject matter of the Amendment. . . .”

Similarly, in *Virginia v. Rives*, 100 U. S. 313, 25 L. Ed. 667, in referring to Section 1 of the Fourteenth Amendment, the Court stated at page 318 of 100 U. S. and at page 669 of 25 L. Ed. that:

“The provisions of the 14th Amendment of the Constitution we have quoted all have reference to state action exclusively, and not to any action of private individuals.”

See also,

United States v. Harris, 106 U. S. 629, 639, 27 L. Ed. 290, 294 and

California Oil and Gas Co. v. Miller, 96 Fed. 12, 22.

All of the Civil Rights Statutes have been construed, as was the Fourteenth Amendment, to provide redress against state action, and not against the invasion of private rights by individuals. These principles, and the authorities establishing them, are summarized in *Love v. Chandler*, 124 F. 2d 785 at 786-787, quotation from which appears as appendix A hereof.

In *Simpson v. Geary*, 204 Fed. 507, the plaintiffs contended that they were deprived of their right to work as brakemen and flagmen by reason of an Arizona law. In holding that no Federal jurisdiction could be invoked on the facts alleged in the complaint, the Court stated as follows:

“The right to contract for and retain employment in a given occupation or calling is not a right secured by the Constitution of the United States, nor by any Constitution. It is primarily a natural right, and it is only when a state law regulating such employment

discriminates arbitrarily against the equal right of some class of citizens of the United States, or some class of persons within its jurisdiction, as, for example, on account of race or color, that the civil rights of such persons are invaded, and the protection of the federal Constitution can be invoked to protect the individual in his employment or calling."

In *Mitchell v. Greenough* (C. C. A. 9), 100 F. 2d 184, 187, that Court, in construing 8 U. S. C. A. 47, stated as follows:

"The prohibition against 'denial of the equal protection of the law' was to prevent class legislation or action."

A lengthy dissertation in accord with the *Chandler* decision will be found in *Love v. United States*, 108 F. 2d 43, 45-46 (cert. denied 309 U. S. 673, 84 L. Ed. 1018), in which the Circuit Court of Appeals for the 8th Circuit said:

"Certain disputes which have arisen on various occasions in the course of our history in respect to the tenure of 'offices' and the power to make removals of incumbents or to replace them with other appointees, have called forth the utmost effort of the courts to find peaceful solution in law and reason. Several such controversies were recognized to be of far-reaching importance. They were justiciable and were settled upon profound consideration by judicial determination.

"But such determination has always been rested upon the interpretation and application of the provisions of the constitution and federal enactments. It cannot be predicated upon any judicial concept concerning an able-bodied, competent and willing man's

natural or inherent right to work. Unless a legal right has been defined and conferred by legislative authority, no justiciable controversy is present. The principles applicable are the same in the field of government work as in the broader field of private enterprise. The right to work at a particular employment must be shown to have become vested by law in the person asserting it. (Citing cases.)"

A case involving the question of the right to practice law and whether it is protected by the Constitution or Statutes of the United States is *Brents v. Stone, et al.*, 60 Fed. Supp. 82, from which we quote as follows on page 84:

"Nor can the action be sustained as one to secure protection of civil rights under the Federal Constitution, for a license to practice law is not a privilege within the purview of any constitutional provision. (Citing cases.)"

To the same effect is:

Emmons v. Smitt, et al., 58 Fed. Supp. 869.

Other decisions which hold adversely to the contention of appellant that the District Court has jurisdiction either under the Fifth or the Fourteenth Amendments to the Federal Constitution or under the Civil Rights Statutes are *Haywood v. United States*, 268 Fed. 795, in which the Circuit Court of Appeals for the Seventh Circuit said at pages 800-801, "to produce, to sell, to contract to sell to any buyer, are not rights or privileges conferred by the Constitution and laws of the United States," and *United States v. Moore*, 129 Fed. 630, in which it was held that the right of a citizen to organize persons in any pursuit

was a fundamental right in all free governments, but was not a right, privilege, or immunity granted or secured to citizens of the United States by its Constitution or laws, and is left solely to the protection of the states.

Schatte, et al. v. International Alilance, etc., et al., 70 Fed. Supp. 1008 at 1010-1011, 165 F. 2d 216, cert. denied 92 L. Ed. 985, the latest decision on the subject, summarizes the applicable law as follows:

“ . . . this court would still be without jurisdiction, since these statutes” (Sec. 41(12), Title 28, Sec. 47(3), Title 8) “were passed to protect individuals from violations of their rights by State action, and none is here alleged. *Love v. Chandler*, 8 Cir., 124 F. 2d 785, 786, 787. Only rights of citizens under the laws of the United States are protected. *Mitchell v. Greenough*, 9 Cir., 100 F. 2d 184, certiorari denied 306 U. S. 659, 59 S. Ct. 788, 83 L. Ed. 1056. That being true, since more than \$3,000 is admittedly involved, this section can in no event confer any jurisdiction not already given by 28 U. S. C. A., Sec. 41(1), which is hereinafter discussed.

“28 U. S. C. A., Sec. 41(1) and 8 U. S. C. A., Sec. 43 provide for redress for deprivations of rights under color of any law, statute, ordinance, regulation, custom, or usage of any State or Territory, in express terms. It is not alleged that the defendants are acting under color of any State law, etc., so these sections cannot act to establish jurisdiction in this court. *Allen v. Corsano*, D. C., 56 F. Supp. 169; *California Oil & Gas Co. v. Miller*, C. C. Cal., 96 F. 12, 22. *Picking v. Pennsylvania R.*, 3 Cir., 151 F. 2d 240, is not applicable here, because the wrongs alleged in that case were all under color of State law.

"The Fifth and Fourteenth Amendments of the Constitution are designed to protect the individual from invasion of his rights, privileges and immunities by the federal and the State governments respectively. *Corrigan v. Buckley*, 271 U. S. 323, 330, 46 S. Ct. 521, 70 L. Ed. 969; *Civil Rights Cases*, 109 U. S. 3, 3 S. Ct. 18, 27 L. Ed. 835. Neither *Hague v. C. I. O.*, 307 U. S. 496, 59 S. Ct. 954, 83 L. Ed. 1423, nor *Screws v. United States*, 325 U. S. 91, 65 S. Ct. 1031, 89 L. Ed. 1495, 162 A. L. R. 1330, has overruled these cases, even by implication, for the wrongs complained of in both the *Hague* and the *Screws* case were committed by the government or under color of law.

* * * * *

"The bare right to work is not a right protected by federal law. *Love v. United States*, 8 Cir. 108 F. 2d 43, certiorari denied 309 U. S. 673, 60 S. Ct. 716, 84 L. Ed. 1018, and cases therein cited; *Brents v. Stone*, D. C., 60 F. Supp. 82, 84; *Emmons v. Smitt*, D. C., 58 F. Supp. 869, affirmed 6 Cir., 149 F. 2d 869, 872."

From the foregoing, it appears clear that the right to contract for and retain employment in a given occupation or calling (*Simpson v. Geary*, *supra*; *Love v. Chandler*, *supra*), the right to be admitted to the practice of law (*Mitchell v. Greenough*, *supra*; *Brents v. Stone*, *et al.*, *supra*; *Emmons v. Smitt*, *et al.*, *supra*), the right to work at a particular employment (*Love v. United States*, *supra*), the right to produce, to sell, to contract to sell to any buyer (*Haywood v. United States*, *supra*), the right to organize persons in any pursuit (*United States v. Moore*, *supra*), or the right to work as a set erector in the Hollywood

Studios under a contract negotiated pursuant to the terms of the National Labor Relations Act (*Schatte, et al. v. International Alliance, etc., et al., supra*), are not rights, privileges, or immunities granted or secured to citizens or residents of the United States by its Constitution or laws; certainly, therefore the "right" to work as a first cameraman in the Hollywood Studios is not such a right.

VII.

No Provision of the California Labor Code Can Vest Jurisdiction in the District Court.

AUTHORITIES:

Labor Code, State of California, Sections 921 to 925;

Shafer v. Registered Pharmacists Union, 16 Cal. 2d 379;

Smith Metropolitan Market Co. v. Lyons, 16 Cal. 2d 389.

Among the statutes and laws relied upon by appellant as vesting jurisdiction in the District Court, are Sections 921 to 925, inclusive, Labor Code, State of California. That the close-shop contract existing between Defendant Local and the Studio employers of first cameramen is valid despite any provision of the California Labor Code is clearly established by numerous decisions of the California Supreme Court, including *Shafer v. Registered Pharmacists Union*, 16 Cal. 2d 379, and *Smith Metropolitan Market Co. v. Lyons*, 16 Cal. 2d 389.

It is elementary that the jurisdiction of District Courts of the United States stems from and is to be found only in the Constitution and statutes of the United States; no state law can enlarge or diminish the scope of such jurisdiction.

VIII.

Requirement in Constitution of the Alliance That Members Be Citizens of the United States or of Canada, or of Any Other Territory in Which the Alliance Exercises Jurisdiction, Is Reasonable and Valid and Violates No Right of Appellant Protected by Any Provision of the Constitution or Laws of the United States; Aliens May Lawfully Be Excluded From Privileges Extended by Law to Citizens.

The foregoing proposition is illustrated by the following examples:

Aliens may be excluded from owning a pool hall business (*Clarke v. Deckebach*, 274 U. S. 392, 71 L. Ed. 1115), from public employment (*Heim v. McCall*, 239 U. S. 173, 60 L. Ed. 206), from taking game as a sportsman (*Patson v. Pennsylvania*, 32 U. S. 183, 58 L. Ed. 539); and they may be denied the right to ownership or interest in the real property of a state (*Terrace v. Thompson*, 263 U. S. 197, 68 L. Ed. 255).

A number of federal statutes preclude aliens from entering into certain activities. Examples of such statutes are as follows:

(1) No radio station license can be granted or held by any alien or the representative of any alien or by any corporation in which more than one-fourth of the directors are aliens or more than one-fourth of the capital stock is owned or voted by aliens, 47 U. S. C. A., Telegraphs, Telephones and Radio Telegraphs, Section 310.

(2) Aliens are precluded from taking animals or birds by use of firearms in the territories and insular possessions of the United States except under a special alien license. In the obtaining of a license to sell or engage in the trade or selling of the skins of fur-bearing animals, an alien is charged a considerably greater license fee than is a resident of the territory involved or a non-resident of the territory who is a citizen of the United States, 48 U. S. C. A., Territories and Insular Possessions, Section 189, Subdivisions (e) and (h).

(3) No alien can homestead federal lands unless he has filed his declaration of intention to become a citizen, 43 U. S. C. A., Public Lands, Section 16.

(4) Aliens may obtain leases and prospecting permits as to federal lands only on a limited basis, 30 U. S. C. A., Mineral Lands and Mining, Section 181.

(5) An alien who has not declared his intention to become a citizen of the United States may not acquire title to any land in the territories of the United States with limited exceptions, 8 U. S. C. A., Aliens and Nationality, Section 71.

The same rule applies to the "acquisition, holding, owning, and disposition of real estate in the District of Columbia," 8 U. S. C. A., Aliens and Nationality, Section 78, and applies, on even a broader basis, in Hawaii, 8 U. S. C. A., Aliens and Nationality, Section 83. No telegraph or cable lines owned or operated or controlled by aliens may

be established in or permitted to enter Alaska, 48 U. S. C. A., Territories and Insular Possessions, Section 302(a).

Moreover, in the interest of the protection of their citizens, the various states have enacted a number of statutory provisions precluding aliens from engaging in activities or occupations that may be entered into by citizens. Examples of such statutory enactments culled from the statutes of the State of California are:

(1) It is provided in Section 118 of the Business and Professions Code that if an alien admitted to practice law fails to become naturalized within a reasonable time after he is eligible, his license shall be revoked on a motion of the attorney general by the district court of appeal which admitted him to practice.

(2) Fishing and hunting license for sporting may be obtained by aliens only upon the payment of license fees greatly in excess of sums required of citizens, Fish and Game Code, Sections 427 and 428.

(3) No alien or person who is not a citizen of the United States may obtain a nursing license unless he has declared his intention to become a citizen of the United States, and if he fails to become a citizen, after having made such declaration, his license shall become void at the end of seven years from the date of filing such declaration of intention, Business and Professions Code, Sections 2736(b), 2743, and 2744.

(4) Aliens are not entitled to old age pensions, Welfare and Institutions Code, Section 2160(b).

(5) No person not a citizen of the United States is eligible for a pharmaceutical license unless he shall have filed and proven his intention to become a citizen. If citizenship is later denied, then his license and privileges are automatically cancelled, Business and Professions Code, Section 4096.

(6) Section 1941 of the Labor Code provides that no person except a citizen shall be employed in any department of the state or any county or city. Section 1943 of the Labor Code provides that no money shall be paid out of the state treasury nor out of the treasury of any county or city to any officer or employee unless such person is a citizen.

(7) Section 1850 of the Labor Code precludes contractors or sub-contractors to employ on any public work any alien except in cases of extraordinary emergency.

In view of the foregoing, it does not seem to us to be open to question that the provisions of the Constitution of The Alliance, a private voluntary association, requiring members to be citizens of the United States, Canada, or territory in which The Alliance exercises jurisdiction, is a reasonable and valid regulation. *However, even if such regulation were deemed arbitrary and discriminatory, such construction thereof would in no manner vest jurisdiction over this action and the parties in the District Court in the absence of diversity of citizenship.*

IX.

Since Defendant Local Has Never Been Nor Professed to Be Bargaining Representative of Appellant and Has Never Undertaken to Bargain for Him, Tunstall Case Doctrine Has No Application.

AUTHORITIES:

Tunstall v. Brotherhood of Locomotive Firemen,
323 U. S. 210, 65 S. Ct. 235, 89 L. Ed. 187;

Steele v. Louisville and N. R. Co., 323 U. S. 192,
65 S. Ct. 226, 89 L. Ed. 173;

Brotherhood of Locomotive Firemen, etc. v. Tunstall (C. C. A. 4th), 163 F. 2d 289.

The Supreme Court of the United States, on the same day in 1944, handed down two decisions (*Tunstall v. Brotherhood of Locomotive Firemen, etc.*, *supra*, and *Steele v. Louisville and N. R. Co.*, *supra*). For convenience, we shall refer to the rule of law enunciated by these decisions as The Tunstall Case Doctrine, which has subsequently been applied in several cases in both the State and Federal courts (*Graham v. Southern Ry. Co.*, 74 Fed. Supp. 663; *Betts v. Easley*, 161 Kan. 459, 169 P. 2d 831, 166 A. L. R. 342), which cases, including the two decisions of the Supreme Court of the United States promulgating The Tunstall Case Doctrine, are, in his opening brief, cited and quoted from by appellant in support of his contention that The Tunstall Case Doctrine is applicable, and that by reason thereof the District Court has jurisdiction of the instant action.

After the Supreme Court had settled the applicable law, the *Tunstall* case, *supra*, went back to the District Court for trial, and subsequently reached the United States Cir-

cuit Court of Appeals for the Fourth Circuit, and is reported as *Brotherhood of Locomotive Firemen, etc. v. Tunstall*, 163 F. 2d 289.

The factual situation forming the basis of The Tunstall Case Doctrine is best expressed in the following language of the Chief Justice, taken from 89 L. Ed. at page 192 (323 U. S. at 211):

“This is a companion case to No. 45, *Steele v. Louisville & N. R. Co.*, decided this day (323 U. S. 192, *ante*, 173, 65 S. Ct. 226) in which we answered in the affirmative a question also presented in this case. The question is whether the Railway Labor Act, 48 Stat. 1185, c. 691, 45 USCA, Secs. 151 *et seq.*, imposes on a labor organization, acting as the exclusive bargaining representative of a craft or class of railway *employees*, the duty to represent all the *employees without discrimination because of their race*. The further question in this case is whether the federal courts have jurisdiction to entertain a non-diversity suit in which petitioner, a railway *employee* subject to the Act, seeks remedies by injunction and award of damages for the failure of the union bargaining representative of his craft to perform the duty imposed on it by the Act, to represent petitioner and other members of his craft *without discrimination because of race*.”

It appears further from the decision in the *Tunstall* case that the Brotherhood of locomotive F. & E. was, pursuant to the Railway Labor Act, *the bargaining agent of the plaintiff therein* and a large number of other Negro *employees* similarly situated. The constitution of the Brotherhood specifically excluded Negroes from membership. *No closed-shop contract existed*. Despite its legal obligation to fairly and without discrimination represent all *em-*

ployees for which it was the bargaining agent, pursuant to the Railway Labor Act, the Brotherhood entered into a contract with the railroad employers which froze Negroes on their present jobs, provided that promotions must be made from a "promotable pool," and that only white persons could thereafter be placed in such "promotable pools." As the Court said in its opinion (89 L. Ed. at 192, 323 U. S. 211-212):

"Petitioner complains of the discriminatory application of the contract provisions to him and other Negro members of his craft in favor of 'promotable,' *i. e.* white, firemen, by which he has been deprived of his pre-existing seniority rights, removed from the interstate passenger run to which he was assigned and then assigned to more arduous and difficult work with longer hours in yard service, his place in the passenger service being filled by a white fireman."

The opinion in the *Tunstall* case adopts the decision rendered the same day in its companion case of *Steele v. Louisville, etc.*, 323 U. S. 192, 65 S. Ct. 226, 89 L. Ed. 173, in which action the plaintiff therein was likewise a Negro and voiced the same complaint as that asserted by *Tunstall*. From that opinion, we learn more of the facts involved in each case, and we quote therefrom in Appendix B hereof.

The foregoing quotations taken from the *Tunstall* and *Steele* cases are sufficient, it seems to us, to clearly establish that the question presented to the Supreme Court of the United States therein bears no resemblance to that

which the instant controversy presents. The distinction between the *Tunstall-Steele* cases and this action may be summarized as follows: (1) In the *Tunstall* case, the Railway Labor Act was involved and no closed-shop contract existed (such a contract being invalid under that Act), whereas in the instant case the National Labor Relations Act is involved and a valid closed-shop contract does exist; (2) in the *Tunstall* case, plaintiff therein was and for a long period of time had been *employed* by the railroad, and *his duly elected bargaining agent* made a contract deliberately discriminating against him solely because of his color, whereas in the instant action appellant is not *employed* in any work classification over which Defendant Local has or asserts jurisdiction, and *Defendant Local is not his bargaining agent*; (3) in the *Tunstall* case, the Brotherhood specifically excluded plaintiff because of color, whereas in the instant case no such arbitrary exclusion is asserted, and exclusion because of lack of citizenship is reasonable and not arbitrary; (4) in the *Tunstall* case (as set forth in 163 F. 2d at 293) when the action was tried on its merits after the Supreme Court had settled the law applicable, the Brotherhood “used its power *as bargaining agent* in violation of the rights of those *for whom it undertakes to bargain* and has thereby inflicted injury upon one of those *whom it professes to represent*,” whereas in the instant case the Defendant Local is not the bargaining agent of appellant and never has and does not now profess to represent him; (5) the Railway Labor Act does not recognize closed-shop con-

tracts (to the contrary, closed-shop contracts are unlawful under the Railway Labor Act (40 Opinion Atty. Gen.—No. 39, Dec. 29, 1942)), whereas same are recognized as valid by the National Labor Relations Act and the Taft-Hartley Act; and (6) by the terms of the National Labor Relations Act (Sec. 2) and Labor-Management Relations Act, 1947 (Sec. 2), employees subject to the Railway Labor Act are specifically excluded.

Since appellant is not, and was not when the closed-shop contracts were executed, employed by any employer with which Defendant Local has or had a closed-shop contract, and since, even as a permittee of Defendant Local, his three assignments, *in* 1945, *in* 1946, and *in* 1947, were not performed at any time when the closed-shop contracts herein were actually executed, he is a stranger to those contracts, a stranger to the Defendant Local, and a stranger to the employers with whom the closed-shop contracts existed and exist. Defendant Local has never represented appellant as bargaining agent and has never professed to so represent him.

As unequivocally appears from the quotations, which we have above or in the Appendix hereto set forth, taken from the *Tunstall-Steele* decisions, jurisdiction is vested in District Courts in actions under the Railway Labor Act against the bargaining agent, designated pursuant to such Act, by *employees*, only when such actions are brought by *employees* discriminated against in a contract negotiated by the bargaining agent professing to represent such *employees* and on whose behalf the bargaining agent

undertook to bargain. Under the National Labor Relations Act (Section 9(a)) and the Labor-Management Relations Act, 1947 (Section 9(a)), it is provided that:

“Representatives designated or selected for the purposes of collective bargaining by the majority of the *employees* in a unit appropriate for such purposes, shall be the exclusive representatives of all of the *employees* in such unit for the purposes of collective bargaining in respect to rates of pay, wages, hours of employment, or other conditions of employment. Provided, that any individual *employee* or a group of *employees* shall have the right at any time to present grievances to their employer, etc.”

It is not open to question, not only from the decisions, but from the language immediately above quoted, which contains no uncertainty or ambiguity and calls for no interpretation or judicial conjecture, that under the National Labor Relations Act and the Labor-Management Relations Act, 1947, a designated or selected bargaining agent represents, undertakes to represent, and professes to represent only employees in the particular unit for which it is such bargaining agent. In the instant case, as appears on the face of the complaint, Defendant Local is the designated bargaining agent of the unit consisting of first cameramen *employed* in the Studios; appellant, not being so employed, is not within that unit; Defendant Local does not represent him and has never undertaken or professed to do so; it is not appellant's bargaining representative and has never represented him in negotiations or made any contract on his behalf.

Furthermore, we submit that even if it be assumed, *arguendo*, first, that the citizenship requirement for applicants for membership in the Defendant Local is, as appellant in his complaint alleges, “unreasonable, arbitrary, capricious and without justification,” and, secondly, that appellant was an employee in the unit of first camera-men within the meaning of the word “employee” as used in the *Tunstall* case; nevertheless, Defendant Local, not being a “company-dominated” labor organization, in negotiating and executing a closed-shop contract, and, subsequently, in refusing appellant membership, *violated no provision of the National Labor Relations Act either as it existed prior to amendment by the Taft-Hartley Act, or thereafter.*

Membership in a *labor organization* by an employee, even though the labor organization has a closed-shop contract covering the work classification in which such employee is engaged, *is not a right granted by the National Labor Relations Act.* Defendant Local, as bargaining representative, had a legal right under the National Labor Relations Act to enter into the closed-shop contracts; Defendant Local, we repeat, as a *labor organization*, is not, and never has been, required under the National Labor Relations Act to admit any person, even though he be an employee, to membership.

The refusal of Defendant Local, as a *labor organization*, to admit appellant to membership cannot be made the basis of litigation, diversity of citizenship being absent, in the District Court below. Whether appellant has ever had, or now has, a cause of action in the California

State Courts under the *James* case rule or before the National Labor Relations Board against Defendant Local in its capacity as a *labor organization*, as distinguished from its capacity as a *bargaining representative*, would be of academic interest only, and for that reason our views thereon are not now expressed.

On page 9 of his opening brief, appellant states that Defendant Local was his “exclusive bargaining agent,” that it violated his rights under the National Labor Relations Act “by refusing to represent him,” “by refusing to treat him on an equal basis with all other first cameramen in the bargaining unit, etc.,” and discriminated against him “as his unwilling representative” on wages, hours, and conditions of employment. Again on page 25 of said brief, appellant states that Defendant Local, “by virtue of statute,” is his “exclusive bargaining agent on wages, hours and working conditions.”

There is no semblance of support in the record for these statements. There is no allegation in the complaint to the effect that Defendant Local ever represented, undertook or professed to represent appellant as his bargaining agent or otherwise; the affirmative facts alleged in the complaint conclusively negate any suggestion that an actual, implied, or professed representation of appellant by Defendant Local ever existed. The erroneous premise contained in the above quoted statements necessarily leads appellant to the equally erroneous conclusion that The Tunstall Case Doctrine is applicable.

X.

Wallace Case Has No Application Because Defendant Local Is Not a Company-Dominated Labor Organization and Appellant Was Not Employed as a First Cameraman by Any Employer, Party to the Closed-Shop Contracts, at the Time Such Contracts Were Executed.

AUTHORITIES:

Wallace Corp. v. National Labor Relations Board,
323 U. S. 248, 65 S. Ct. 238, 89 L. Ed. 216;

Tenth Annual Report, National Labor Relations Board, 57-58;

Twelfth Annual Report, National Labor Relations Board, 49-50.

Finally, appellant contends that the District Court below has jurisdiction under the rule of law enunciated by the Supreme Court of the United States in *Wallace Corp. v. National Labor Relations Board*, 323 U. S. 248, 65 S. Ct. 238, 89 L. Ed. 216.

The *Wallace* case reached the Supreme Court of the United States on writ of certiorari to the United States Circuit Court of Appeals for the Fourth Circuit to review judgments enforcing orders of the National Labor Relations Board in an unfair labor practice proceeding. Two competing labor organizations were contending for the right to represent the employees of the Wallace Corporation. Pursuant to an agreement, a consent election was held and the Independent union was certified by the Board as bargaining representative. The company then signed a union shop contract with Independent with the knowledge that Independent intended, by refusing membership to the C. I. O. (defeated union) *employees*, to oust them

from their jobs. Independent thereupon refused to admit C. I. O. men to membership and the company discharged them. We quote from page 224, 89 L. Ed., 223 U. S., page 250, as follows:

“In a subsequent unfair labor practice proceeding the Board found that (1) Independent had been set up, maintained, and used by the petitioner” (employer) “to frustrate the threatened unionization of its plant by the C. I. O., and (2), the union shop contract was made by the company with knowledge that Independent intended to use the contract as a means of bringing about the discharge of former C. I. O. employees by denying them membership in Independent. The Board held that the conduct of the company in both these instances constituted unfair labor practices. It entered an order requiring petitioner to disestablish Independent, denominated by it a ‘company union’; to cease and desist from giving effect to the union shop contract between it and Independent; and to reinstate with back pay forty-three employees, found to have been discharged because of their affiliation with the C. I. O., and because of their failure to belong to Independent, as required by the union shop contract.”

As appears from the foregoing, the parties aggrieved were, *at the time Independent was elected bargaining representative* of all the *employees*, and for a long time prior thereto had been, *employees* of the company with which the union shop contract was executed, and, what is far more important, that Independent was at the time a company-dominated labor organization; in the instant case, appellant was not an employee (first cameraman) of any of the Hollywood Studios at the time any of the closed-shop contracts referred to in the complaint were executed,

In the *Wallace* case, the labor organization involved (Independent) by operation of law became the bargaining representative of all employees, including those not holding membership, in it, and by reason of the contract which it executed, coupled with its refusal to admit such non-member employees into membership, deprived them of their existing employment; in the instant case, appellant was not an employee and Defendant Local was never his bargaining representative by operation of law or otherwise. Furthermore, the controlling distinction between the *Wallace* case and the instant action is that in the *Wallace* case the labor organization was company dominated, whereas in the instant action appellant expressly alleges that Defendant Local “is *not* established, maintained or dominated by any employer” [7]. Under the National Labor Relations Act (Wagner Act) and under its successor, the Labor-Management Relations Act, 1947 (Taft-Hartley Act), the right on the part of a labor organization as the bargaining representative of employees to enter into a closed-shop contract is expressly forbidden when the labor organization is “established, maintained or assisted” by the company with which such contract is made (Section 8(3)), National Labor Relations Act and Labor-Management Relations Act, 1947). Where, however, the labor organization is not “company dominated,” a closed-shop contract entered into by it is, by both Acts, specifically recognized as valid.

The meaning and effect of the *Wallace* case decision is succinctly set forth in the Tenth Annual Report of the National Labor Relations Board [57-58], from which we quote as follows:

“*Wallace Corp. v. N. L. R. B.*, 323 U. S. 248, decided December 18, 1944. In this case the Court up-

held the Board's determination that a closed-shop contract made with a *company-dominated union* was invalid and that *discharges* made pursuant to the contract violated Section 8(3) of the Act.

* * * * *

“* * * The Court held that while *the Act sanctions closed-shop contracts*, the employer could not, in cooperation with the union, utilize such a contract to penalize *groups of its employees* because of prior union membership without violating the provisions of the Act which guarantee the right of self-organization and prohibit discrimination on account of the exercise of that right.

* * * * *

“This is the first case under the Wagner Act which presented the Court with an opportunity to define the responsibilities of a collective bargaining agent toward *minority groups in the unit* which under the prevailing principle of majority rule it has exclusive power to represent. The Court laid down these principles: A collective bargaining representative selected by a majority of the *employees* in a unit is the agent of all *employees* and must represent their interests impartially and without discrimination; this duty is violated where the bargaining agent enters into a closed-shop contract with the employer with the declared intention of denying membership to the *former adherents of a rival union* in order to obtain their *discharge* by the employer. The Court's declaration in the *Wallace* case concerning the obligations of a bargaining agent must be compared with its similar holdings in the companion cases of *Steele v. L. & N. R. Co.*, 323 U. S. 192, and *Tunstall v. Brotherhood*, 323 U. S. 210. These cases, decided contemporaneously with the *Wallace* case, involved dis-

crimination by railway labor organizations against *employees* of the Negro race. The three cases, the Court subsequently stated (*Hunt v. Grumbach*, 65 S. Ct. 1545), 'stand for the principle that a bargaining agent owes a duty not to discriminate unfairly against any of the group it *purports to represent*.' "

In the Twelfth Annual Report of the National Labor Relations Board, pages 49-50, we find these further references to the *Wallace* case as follows: "The principle announced by the Supreme Court in *Wallace Corp. v. N. L. R. B.* * * * that a closed-shop proviso does not sanction the *discharge* of *employees* whom the contracting union has expelled for the purpose of penalizing them for their activities on behalf of a rival union, etc.," and "the *Wallace* case was concerned with a closed-shop contract made and utilized by the contracting union for the purpose of eliminating from its membership *employees* who had previously opposed it."

On pages 7 and 8 of his opening brief, appellant, apparently for the purpose of endeavoring to persuade this Court that the District Court below has jurisdiction of this action either under The Tunstall Case Doctrine or the doctrine of the *Wallace* case—or a blend of both doctrines concocted by appellant—quotes from the dissenting opinion of Mr. Justice Jackson in *Trailmobile Co. v. Whirls*, 331 U. S. 40, 67-68, 67 S. Ct. 982, 995-996, 92 L. Ed. 1328, 1345. We concede that even a dissenting opinion of such a distinguished jurist as Mr. Justice Jackson is entitled to great respect, but it, nevertheless, remains a dissenting opinion. There are, however, two phrases in the quotation set forth by appellant which we believe should be emphasized, namely, "*those who undertake to act for*

others,” and “*assumed to represent*,” appearing in the sentence reading as follows: “Courts from time immemorial have held that *those who undertake to act for others* are held to good faith and fair dealing and may not favor themselves at the cost of those they have *assumed to represent*.” We reiterate, in order to emphasize, that Defendant Local did not at any time “undertake to act” for appellant and has not at any time “assumed to represent” him.

If a basis exists for charges by appellant against the Hollywood Studios of unfair labor practices, under the doctrine of the *Wallace* case, despite the fact that Defendant Local is not a “company-dominated labor organization,” that matter would be within the exclusive jurisdiction of the National Labor Relations Board; if appellant is of the opinion that the factual matters alleged in his complaint constitute unfair labor practices on the part of Defendant Local under the Labor-Management Relations Act, 1947, it is the National Labor Relations Board, and not District Courts of the United States, which likewise possesses exclusive jurisdiction thereof. (*Amazon Mills Co. v. Textile Workers Union* (C. C. A. 4th, 1948), 167 F. 2d 183; *Donnelly Garment Co. v. International Ladies’ Garment Workers Union*, 99 F. 2d 309; *Gerry of California v. Superior Court*, 32 A. C. 141, 194 P. 2d 689.)

From “prior to 1941,” [6]—while appellant was still a resident of Poland and before he had even entered the United States [9]—and continuously down to the present time, closed-shop contracts covering first cameramen in the California motion picture studios have been and now are in effect, originally “from prior to 1941 to until the

end of 1942" [6] with ASC, from "on or about January 1, 1943, to and including the date of the filing of this complaint" [8] with Defendant Local, and the last closed-shop contract "was executed in writing as of January 1, 1946, for a term ending December 31, 1948," with Defendant Local [8].

The condition of which appellant complains existed on and before his arrival in this country; it is thus he found it and it has not since changed.

Conclusion.

Appellees Defendant Local and Aller respectfully submit that the judgment of the District Court should be affirmed.

Respectfully submitted,

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APPENDIX A.

Love v. Chandler, 124 F. 2d 785 at 786-787:

“The appellant contends that his complaint states a claim under Sec. 47(2) and (3) of Title 8, U. S. C. A., authorizing actions for damages for conspiracies to deprive citizens of the equal protection of the laws or from exercising any right or privilege as a citizen of the United States, and that it also states a claim under Sec. 48 of Title 8, U. S. C. A., which authorizes the recovery of damages from any person who, having knowledge of such a conspiracy and the power to prevent it, neglects or refuses so to do. The appellant further contends that the trial court had jurisdiction of the subject matter of this action by virtue of Sec. 41(12), (13) and (14) of Title 28, U. S. C. A., which confer upon the District Courts of the United States jurisdiction of actions to recover damages for deprivation of rights in furtherance of such conspiracies as are described in Sec. 47 of Title 8, U. S. C. A.

“The trial court was of the opinion that, since this Court had held in *Love v. United States*, 108 F. (2d) 43, 49, that the right of the appellant to be employed by the Works Progress Administration was not an absolute right conferred by the Constitution or laws of the United States and that the District Court was without jurisdiction to review the administrative action of which the appellant had complained in that case, the complaint in the instant action, under the

rule announced in *Mitchell v. Greenough*, 9 Cir., 100 F. (2d) 184, certiorari denied 306 U. S. 659, 59 S. Ct. 788, 83 L. Ed. 1056, did not state a claim for damages resulting from a conspiracy to deprive the appellant of any right or privilege dependent upon a law of the United States.

“The statutes which the appellant seeks to invoke were passed shortly after the Civil War to aid in the enforcement of the Thirteenth Amendment prohibiting State action the effect of which would be to abridge the privileges or immunities of citizens of the United States or to deprive any person of life, liberty or property without due process or to deny any person the equal protection of the law, and the Fifteenth Amendment prohibiting the denial of the right to vote on account of race or color. (Citing cases.) The statutes were intended to provide for redress against State action and primarily that which discriminated against individuals within the jurisdiction of the United States. (Citing cases.) The statutes, while they granted protection to persons from conspiracies to deprive them of the rights secured by the Constitution and laws of the United States (*United States v. Mosley*, 238 U. S. 383, 387, 388, 35 S. Ct. 904, 59 L. Ed. 1355), did not have the effect of taking into federal control the protection of private rights against invasion by individuals. (Citing cases.) The protection of such rights and redress for such wrongs was left with the States. (Citing cases.)

“The appellant does not seek redress because the State of Minnesota is discriminating against him, or because its laws fail to afford him equal protection. We have already held that *he had no absolute* right under the laws of the United States to have or retain employment by the Works Progress Administration. The appellant seeks damages because certain persons, as individuals, have allegedly conspired to injure him and have injured him by individual and concerted action. The wrongs allegedly suffered by the appellant are assault and battery, false imprisonment, *and interference with his efforts to obtain and retain employment with the Works Progress Administration.* The protection of the rights allegedly infringed and redress for the alleged wrongs are, we think within the exclusive province of the State. (Citing cases.) We agree with the trial court that the appellant has failed to state a claim upon which relief could be granted under the statutes which he has invoked. His complaint was properly dismissed.”

APPENDIX B.

Steele v. Louisville, etc., 323 U. S. 192 at 194, 89 L. Ed. 173 at 179:

“The allegations of the bill of complaint, so far as now material, are as follows: Petitioner, a Negro, is a locomotive fireman *in the employ of respondent railroad*, suing on his own behalf and *that of his fellow employees* who, like petitioner, are Negro firemen employed by the Railroad. Respondent Brotherhood, a labor organization, is, as provided under Sec. 2, Fourth of the Railway Labor Act, the exclusive bargaining representative of the *craft of firemen employed* by the Railroad and is recognized as such by it and the members of the craft. The majority of the firemen *employed* by the Railroad are white and are members of the Brotherhood, but a substantial minority are Negroes who, by the constitution and ritual of the Brotherhood, are excluded from its membership. As the membership of the Brotherhood constitutes a majority of all firemen *employed* on respondent Railroad, and as under Sec. 2, Fourth the members because they are the majority have the right to choose and have chosen the Brotherhood to represent the craft, petitioner and other Negro firemen on the road have been required to accept the Brotherhood as their representative for the purposes of the Act.

“On March 28, 1940, the Brotherhood, purporting to act as representative of the entire craft of fire-

men, without informing the Negro firemen or giving them opportunity to be heard, served a notice on respondent Railroad and on twenty other railroads operating principally in the southeastern part of the United States. The notice announced the Brotherhood's desire to amend the existing collective bargaining agreement in such manner as ultimately to exclude all Negro firemen from the service. By established practice on the several railroads so notified only white firemen can be promoted to serve as engineers, and the notice proposed that only 'promotable,' *i. e.*, white, men should be employed as firemen or assigned to new runs or jobs or permanent vacancies in established runs or jobs.

* * * * *

" . . . On May 12, 1941, the Brotherhood entered into a supplemental agreement with respondent Railroad further controlling the seniority rights of Negro firemen and restricting their *employment*. The Negro firemen were not given notice or opportunity to be heard with respect to either of these agreements, which were put into effect before their existence was disclosed to the Negro firemen.

* * * * *

" . . . The Brotherhood has acted and asserts the right to act as exclusive bargaining representative of the firemen's craft. It is alleged that in that capacity it is under an obligation and duty imposed by the

Act to represent the Negro firemen impartially and in good faith; but instead, in its notice to and contracts with the railroads, it has been hostile and disloyal to the Negro firemen, has deliberately discriminated against them, and has sought to deprive them of their seniority rights and to drive them out of *employment in their craft*, all in order to create a monopoly of employment for Brotherhood members.

* * * * *

“The labor organization chosen to be the representative of the craft or class of *employees* is thus chosen to represent all of its members, regardless of their union affiliations or want of them.”

No. 11972

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

CURTIS COURANT,

Appellant,

vs.

INTERNATIONAL PHOTOGRAPHERS OF THE MOTION PIC-
TURE INDUSTRY LOCAL 659, ETC., *et al.*,

Appellees.

Answering Brief of Appellee International Alliance of
Theatrical Stage Employes and Moving Picture
Machine Operators of the United States and
Canada.

BODKIN, BRESLIN & LUDDY,

HENRY G. BODKIN,

GEORGE M. BRESLIN,

MICHAEL G. LUDDY,

1225 Citizens National Bank Building, Los Angeles 13,
Attorneys for Appellee The Alliance.



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I.

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No. 11972

IN THE

United States Court of Appeals

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CURTIS COURANT,

Appellant,

vs.

INTERNATIONAL PHOTOGRAPHERS OF THE MOTION PICTURE INDUSTRY LOCAL 659, ETC., *et al.*,

Appellees.

Answering Brief of Appellee International Alliance of Theatrical Stage Employes and Moving Picture Machine Operators of the United States and Canada.

Additional Statement of the Case.

Appellee International Alliance of Theatrical Stage Employes and Moving Picture Machine Operators of the United States and Canada, hereinafter referred to as The Alliance, a voluntary unincorporated association, is an international labor union and the parent organization of appellee International Photographers of the Motion Picture Industry Local 659, etc., hereinafter called Defendant Local. Defendant Local, an autonomous labor organization, is chartered by The Alliance. When on August 28, 1939, as appears in Paragraph IV of the complaint herein

[5-6*], The Alliance was certified by the National Labor Relations Board as the exclusive bargaining agency for all of its members engaged in the production of motion pictures, the work classification of first cameramen was expressly excluded from such certification. At that time first cameramen were members of the American Society of Cinemaphotographers (ASC) and were not members of The Alliance or Defendant Local. It appears further from the complaint [6-7] that until on or about December 10, 1942, the American Society of Cinemaphotographers (ASC) was the designated representative for collective bargaining of first cameramen, and that ever since December 10, 1942, appellee Defendant Local has, by designation, been the recognized exclusive bargaining agent of such first cameramen. The closed-shop contracts described in the complaint were all executed by Defendant Local; The Alliance was not a party thereto.

It thus appears that appellee The Alliance has never at any time been the bargaining representative of first cameramen, and that it was not a party to any of the closed-shop contracts which form the basis of appellant's complaint.

*Figures appearing in brackets refer, unless otherwise noted, to pages of Transcript of Record.

I.

Motion of Appellee The Alliance to Dismiss Was Properly Granted Because, as Appears Upon the Face of the Complaint, It, Not Being Either the Certified or Recognized Bargaining Agent of First Cameramen Nor a Party to the Closed-shop Contracts Involved, Is Not a Necessary or Proper Party Defendant, and the Complaint Does Not State a Claim Against It Upon Which Relief Can Be Granted.

Appellee The Alliance adopts as its own the answering brief filed herein by appellees International Photographers of the Motion Picture Industry Local 659, etc., and Herbert Aller.

In addition, it directs the attention of this Court to the fact that it has never been either the certified or designated bargaining representative of first cameramen, and was not a party to any of the closed-shop contracts involved in this litigation. Hence, the District Court below was without jurisdiction, and the complaint fails to state a claim upon which relief can be granted against The Alliance and in favor of appellant.

Conclusion.

Appellee The Alliance respectfully submits that the judgment of the District Court should be affirmed.

Respectfully submitted,

BODKIN, BRESLIN & LUDDY,

HENRY G. BODKIN,

GEORGE M. BRESLIN,

MICHAEL G. LUDDY,

Attorneys for Appellee The Alliance.



No. 11972

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

CURTIS COURANT,

Appellant,

vs.

INTERNATIONAL PHOTOGRAPHERS OF THE MOTION PICTURE INDUSTRY, LOCAL 659, etc., *et al.*,

Appellees.

REPLY BRIEF OF APPELLANT.

HENRY B. ELY,

1215 Citizens National Bank Building, Los Angeles 13,

Attorney for Appellant.

FILED

JAN 14 1949



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INTERNATIONAL PHOTOGRAPHERS OF THE MOTION PICTURE INDUSTRY, LOCAL 659, etc., *et al.*,

Appellees.

REPLY BRIEF OF APPELLANT.

Introduction.

Appellees have completely failed to meet the contention of appellant that his claim is in part founded upon Section 7 of the National Labor Relations Act, granting him the right to join labor organizations (see App. Op. Br. pp. 2, 4, 5, 14, 36 and 43). It has been distinctly held that such a right was granted under the National Labor Relations Act.

“Although the shipbuilding industry may affect interstate commerce and therefore may be subject to the provisions of the National Labor Relations Act (49 Stats. 449; 29 U. S. C. A. §§151-166), there is nothing in the act that gives the defendant unions a right to maintain a closed or partially closed member-

ship together with a closed shop agreement. To the contrary, a reasonable interpretation of the statute, together with its underlying policy, would seem to require that unions chosen to represent the employees must be open to all who wish to join.”

James v. Marinship Corp., 25 Cal. 2d 721, 735, 155 P. 2d 329.

“The union defendants next contend that the trial court did not have jurisdiction over the subject matter because, they assert, if an injunction were granted it would in effect destroy their closed shop contract and affect the status of the employees of the shipyards, and it would thus interfere with the rights of collective bargaining granted by the National Labor Relations Act. * * * That act clearly does not give a union the authority to maintain a closed shop agreement together with an arbitrarily closed union membership. Moreover, the rights which plaintiffs seeks to enforce not only are consistent with the provisions of the federal act but appear to be affirmatively granted thereby.”

Williams v. Int. etc. of Boilermakers, 27 Cal. 2d 586, 593, 165 P. 2d 903.

The same rule applies under the Railway Labor Act:

“* * * a union acting as the exclusive bargaining agent under the law, for all employees, cannot act arbitrarily, cannot deny equality of privilege, to individuals or minority groups merely because membership in the organization is voluntary. To hold otherwise would do violence to basic principles of our American system.”

Betts v. Easley, 161 Kan. 459, 166 A. L. R. 342, 351, 169 P. 2d 831.

Appellant hereinafter briefly responds to the Answering Brief of Appellees Local 659, etc. and the numbered points correspond to the points of Appellees in their brief.

I.

Appellant makes no contention that the ordinary fraternal lodge would be subject to the limitations of our Treaty with Poland or the Charter of the United Nations. Appellant does contend that appellees acting as exclusive bargaining representatives by virtue of the National Labor Relations Act, are agencies functioning under Federal powers and, until Congress specifically authorizes them to violate United States treaties, they are bound by such treaties, as would be any other governmental agency whether State or Federal.

“We think that the Railway Labor Act imposes upon the statutory representative of a craft at least as exacting a duty to protect equally the interests of members of the craft as the Constitution imposes upon a legislature to give equal protection to the interests of those for whom it legislates. Congress has seen fit to clothe the bargaining representative with powers comparable to those possessed by a legislative body both to create and restrict the rights of those whom it represents, *cf. J. I. Case Co. v. National Labor Relations Board, supra*, 321 U. S. 335, 64 S. Ct. 579, but it has also imposed on the representative a corresponding duty.”

Steele v. Louisville & N. R. Co., 65 S. Ct. 226, 232, 323 U. S. 192, 202.

“In the light of the history and purpose of the Act, as construed in many decisions, the trial court’s view that the acts complained of are solely those of ‘a private association of individuals’ is wholly untenable. The acts complained of are those of an organization acting as an agency created and functioning under provisions of Federal law. This being true, it is unnecessary to consider appellees’ contention that the Fifth Amendment is not here applicable because it relates only to action by the Federal government and not to acts of private persons.”

Betts v. Easley, 161 Kan. 459, 166 A. L. R. 342,
350, 169 P, 2d 831.

II.

Appellant does not dispute the principle of law set forth under this numbered point of the Answering Brief of Appellees Local 659, etc., but has argued throughout his Opening Brief that a substantial question involving the construction and effect of Federal laws is the subject matter of this action.

III.

The Anti-Trust laws as set forth on page 10 of the Answering Brief of Appellees Local 659, etc., provides that nothing “shall restrain members of such organizations from lawfully carrying out the legitimate objects thereof.” The appellant contends that the monopoly of the appellees in excluding all non-members from their union and not permitting them to work to prevent competition is to be condemned under the Anti-Laws laws just as much as a similar practice by an association of business men.

Hunt v. Crumboch, 325 U. S. 821, 65 S. Ct. 1545, 89 L. Ed. 1954, is not similar to the present case.

IV.

Point IV of the Answering Brief of Appellees Local 659, etc., is similar to their point II. If the National Labor Relations Act does not regulate commerce then many cases upholding its constitutionality must be overruled. The real question again is whether substantial rights are involved under that Act, the Treaties, and other Acts set forth in Appellant's Opening Brief.

V.

Appellees Local 659, etc., claim under their point V that no jurisdiction in the type of case considered was specifically given to the Federal courts by the terms of the National Labor Relations Act of 1935. This is unquestionably true, but we again emphasize that we are concerned whether any other Federal rights have been infringed by the appellees and, if so, whether under the case of *Stark v. Wickard*, 321 U. S. 288, 64 S. Ct. 559, 88 L. Ed. 733 (cited in App. Op. Br. p. 44), the Federal courts may give appropriate relief in the exercise of their general jurisdiction.

Appellees do not claim that the National Labor Relations Board could have given appellant any administrative relief under the National Labor Relations Act of 1935, so therefore, the appellant is properly in the Federal court as to that portion of his complaint occurring prior to the effective date of the Labor Management Relations Act of 1947. This latter Act did not release or extinguish any liabilities incurred under the original Act. *N. L. R. B. v. Mylan-Sparta Co.* (C. C. A. 6), 166 F. 2d 485, 488.

Upon the allegations as set forth in the complaint, the National Labor Relations Board under the Labor Management Relations Act of 1947, has no jurisdiction

or authority to give any relief to appellant because no overt acts tantamount to unfair practices for labor organizations have been alleged by the appellant from the time of the effective date of the Labor Management Relations Act of 1947. Before the National Labor Relations Board is given jurisdiction to take steps against a union under the 1947 Act, the union must have committed an act or practice. (Title I, Section 101 (b) (j) (k) and (l), Labor Management Relations Act of 1947, 29 U. S. C. A. 160 (b) (j) (k) and (l).) Therefore, since no unfair labor practice is alleged subsequent to the effective date of the Labor Management Relations Act of 1947, the National Labor Relations Board has no jurisdiction to proceed against appellees and appellant has no administrative remedy.

VI.

Appellant has not argued in his Opening Brief that the Civil Rights Statutes protect him in this case.

VII.

Appellant has not argued in his Opening Brief that the California Labor Code vested jurisdiction in the District Court.

VIII.

Whatever may be the opinion of appellees concerning the effect of *Oyama v. State of California*, 332 U. S. 633, 68 S. Ct. 269, on the right of aliens ineligible to citizenship to hold land, the State of California is now convinced that under the *Oyama* case such aliens can hold California lands, having agreed to reverse judg-

ments providing for escheat of such lands. *People v. Fugita*, 31 Cal. 2d 872, 192 P. 2d 948; *People v. Federal Land Bank*, 31 Cal. 2d 871, 192 P. 2d 948. Furthermore, there appears no doubt today that a State agency cannot prevent aliens ineligible to citizenship from carrying on the common occupations of life such as fishing in its coastal waters. *Takahashi v. Fish and Game Commission*, 334 U. S. 410, 68 S. Ct. 1138, 92 L. Ed. (Adv. Ops.) 1096.

Appellant has specifically alleged that the Constitution of Appellee IATSE is unreasonable, arbitrary, capricious and without jurisdiction [Tr. 23], and the Motion to Dismiss admits all properly pleaded matters in the complaint. However, all recent decisions of the Supreme Court of the United States have struck down every attempt at discrimination by such agencies as labor unions and State agencies. If the appellees, acting under Federal powers, were specifically authorized by Congress to exclude aliens, an entirely different question might be involved. No such authorization appears and it is just as unthinkable for the appellees to discriminate because of citizenship as for any Governmental agency to do so when not specifically authorized by Congressional authority.

IX.

It appears to appellant that appellees have misinterpreted the various cases setting forth the duties of collective bargaining agencies who are the exclusive representatives of all employees under the National Labor Relations Act.

Appellees having undertaken to act for *a majority* of the members of the craft are required, even against their own will, to act on behalf of *all*.

“So long as a labor union assumes to act as the statutory representative of a craft, it cannot rightly refuse to perform the duty, which is inseparable from the power of representation conferred upon it, to represent the entire membership of the craft.”

Steele v. Louisville & N. R. Co., 323 U. S. 192, 204,
65 S. Ct. 226, 233.

Other cases setting forth the principle that the union as exclusive bargaining representative must act on behalf of all in the craft are referred to in pages 14 through 27 of Appellant's Opening Brief.

X.

Appellees contend under point X of their Answering Brief that the doctrine set forth in *Wallace Corporation v. N. L. R. B.*, 323 U. S. 248, 65 S. Ct. 238, 89 L. Ed. 216, is confined to company dominated unions. Numerous cases decided by the Federal and State courts have not so limited the *Wallace* case. A recent case is *Colonie Fibre Co. v. N. L. R. B.* (C. C. A. 2), 163 F. 2d 65, where an A. F. of L. union not dominated by the employer caused the discharge of an employee because of his failure to maintain membership in that union.

The second part of this point of appellees is that appellant was not an employee at the time the closed shop contracts were entered into. Appellees state:

“The condition of which appellant complains existed on and before his arrival in this country; it is thus he found it and it has not since changed.”
(Answering Brief of Appellees, page 49.)

We believe this point is answered by the following quotation in the *Wallace* case:

“The duties of a bargaining agent selected under the terms of the Act extend beyond the mere representation of the interests of its own group members. By its selection as bargaining representative, it has become the agent of all the employees, charged with the responsibility of representing their interests fairly and impartially. Otherwise, employees who are not members of a selected union at the time it is chosen by the majority would be left without adequate representation.”

Wallace Corporation v. N. L. R. B., 323 U. S. 248, 255, 256, 65 S. Ct. 238, 241, 242.

Respectfully submitted,

HENRY B. ELY,

Attorney for Appellant.



No. 11973

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

E. C. SIMMONS,

Appellant,

VS

HARRY C. WESTOVER, Collector of Internal Revenue,

Appellee.

TRANSCRIPT OF RECORD

Upon Appeal From the District Court of the United States
for the Southern District of California
Central Division

FILED

AUG 28 1948

PAUL P. O'BRIEN,
CLERK

No. 11973

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

E. C. SIMMONS,

Appellant,

vs

HARRY C. WESTOVER, Collector of Internal Revenue,

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In the District Court of the United States
In and For the Southern District of California
Central Division

No. 5517-W Civil

E. C. SIMMONS,

Plaintiff,

v.

HARRY C. WESTOVER, Collector of Internal Revenue,
Defendant.

COMPLAINT FOR REFUND OF INCOME TAXES
PAID

Plaintiff, E. C. Simmons, by Latham & Watkins, his attorneys, presents this, his Complaint against the defendant herein, and for cause of action alleges as follows:

I.

Plaintiff, E. C. Simmons, resides at Beverly Hills, in the County of Los Angeles, State of California.

II.

Defendant, Henry C. Westover, was, on and subsequent to November 14, 1945, and still is, the duly appointed and acting Collector of Internal Revenue of the United States for the 6th District of California.

III.

This is a suit filed pursuant to the provisions of Section 24(20) of the Judicial Code as amended (28 U. S. C. A., Sec. 41(20)), [2] for the recovery of Federal income taxes erroneously and illegally collected from the plaintiff for the calendar year 1925 in the amount of \$1,255.18 and interest erroneously and illegally collected therewith in the

amount of \$1,904.09, together with interest on the total amount of \$3,159.27.

IV.

On or about June 5, 1929, the plaintiff executed an "Agreement as to Final Determination of Tax Liability" for the years 1925, 1926, and 1927 in the principal sum of \$8,869.72 and agreed to the assessment of any deficiency included therein, and on or about October 23, 1929, said agreement was approved and accepted by the Commissioner of Internal Revenue. Of said principal sum, there remained unpaid from and after August 15, 1933, a balance of \$1,255.18.

V.

On or about November 14, 1945, plaintiff paid to the defendant herein, in response to said defendant's notice and demand therefor, said balance of \$1,255.18, together with interest in the amount of \$1,904.09, or a total of \$3,159.27.

VI.

More than six (6) years had elapsed between the date of the assessment mentioned in paragraph IV and the date of payment mentioned in paragraph V, to wit: more than sixteen (16) years.

VII.

The collection of said tax and interest was barred after six years from the date of said assessment pursuant to the provisions of Section 276(c) of the Internal Revenue Code (26 U. S. C. A., Sec. 276(c)).

VIII.

On December 11, 1945, plaintiff filed with the defendant, as Collector of Internal Revenue, at Los Angeles,

California, a claim for refund in the amount of \$3,159.27, plus interest, [3] representing the tax and interest paid by him as alleged in paragraph V for said year 1925. A true copy of said claim and of the statement attached thereto is hereto attached, marked "Exhibit A" and is by reference made part of this Complaint.

IX.

More than six (6) months have elapsed since the filing of said claim and no decision has been rendered thereon.

Wherefore, plaintiff prays that a judgment may be entered herein in favor of the plaintiff and against the defendant for \$3,159.27, plus interest thereon, from November 14, 1945, at 6% per annum, together with costs of suit, and for such other and further relief as to the Court may seem proper.

LATHAM & WATKINS

By Richard W. Lund

Attorneys for Plaintiff

1112 Title Guarantee Building

Los Angeles 13, California [4]

[Verified.]

"EXHIBIT A"

Form 843

Treasury Department
Internal Revenue Service
(Revised April 1940)

CLAIM

To Be Filed With the Collector Where Assessment Was
Made or Tax Paid

Collector's Stamp
(Date received)

The Collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

- ☐ Refund of Tax Illegally Collected.
- ☐ Refund of Amount Paid for Stamps Unused, or Used in Error or Excess.
- ☐ Abatement of Tax Assessed (not applicable to estate or income taxes).

State of California

County of Los Angeles—ss:

[Type or Print] Name of taxpayer or purchaser of stamps E. C. Simmons.

Business address 540 North La Brea Avenue, Los
(Street)

Angeles 36, California.

(City) (State)

Residence

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

1. District in which return (if any) was filed Sixth California.
2. Period (if for income tax, make separate form for each taxable year) from January 1, 1925, to December 31, 1925.
3. Character of assessment or tax—Income tax and interest thereon.
4. Amount of assessment, \$3,159.27; dates of payment November 14, 1945.
5. Date stamps were purchased from the Government....
6. Amount to be refunded \$3,159.27.

7. Amount to be abated (not applicable to income or estate taxes)..... \$.....
8. The time within which this claim may be legally filed expires, under Section 322(b)(1) of the Internal Revenue Code on November 14, 1947.

The deponent verily believes that this claim should be allowed for the following reasons:

See statement attached. [5]

* * * * *

E. C. SIMMONS CLAIM FOR REFUND

On November 14, 1945, the taxpayer paid, under protest, to the Collector of Internal Revenue at Los Angeles, California, in response to a demand therefor, additional income taxes for the calendar year 1925 in the amount of \$1,255.18 together with interest thereon in the amount of \$1,904.09, or a total of \$3,159.27.

Said tax and interest was not collected within six years after assessment nor within a reasonable time after the rejection of taxpayer's offer in compromise filed in 1933 at which time he agreed that the tax might be collected by distraint or by a proceeding in court begun at any time.

The collection of said tax and interest was, therefore, barred by the provisions of Section 276(c), I. R. C., and the payment made constitutes an overpayment as defined by Section 3770(a)(2), I. R. C.

Accordingly, said payment is to be refunded to the taxpayer and, for that purpose, this claim is filed.

[Endorsed]: Filed Jun. 27, 1946. Edmund L. Smith, Clerk. [6]

[Title of District Court and Cause]

ANSWER

The defendant in answer to plaintiff's complaint herein admits, denies and alleges:

I.

Admits the allegations contained in Paragraph I thereof.

II.

Admits the allegations contained in Paragraph II thereof.

III.

Admits the allegations contained in Paragraph III thereof, except that it is denied that the collection of the taxes and interest involved was erroneous or illegal.

IV.

Admits the allegations contained in Paragraph IV of the complaint.

V.

Admits the allegations contained in Paragraph V of the complaint.

VI.

No answer is made to Paragraph VI thereof since Paragraph IV, to which [7] reference is made in Paragraph VI, does not mention an assessment made but only an agreement that an assessment may be made in the future.

VII.

Denies the allegations contained in Paragraph VII of the complaint, and alleges that in and by the "Agreement as to Final Determination of Tax Liability" executed between the plaintiff and the Government as alleged in Para-

graph IV of the complaint, the plaintiff agreed to a deficiency in his income tax for the year 1925 in the amount of \$5,281.66; that pursuant to the Agreement, income taxes in the amount of \$5,281.66 were assessed against the plaintiff on October 19, 1929, together with interest thereon in the amount of \$1,053.36, a total of \$6,335.02 for the year 1925; that pursuant to the Agreement, the Commissioner of Internal Revenue determined overassessments for 1926 of \$795.45 and for 1927 of \$2,067.57, and that such overassessments were, with the consent of the plaintiff, credited against the deficiency for 1925, leaving an outstanding balance of \$3,472.06; that thereafter payments were made by plaintiff during the period 1930-1934, which reduced the balance to \$1,255.18; that on August 15, 1932, plaintiff filed an offer in compromise (Form 656) with the Collector of Internal Revenue at Los Angeles, California, in the amount of \$250, payable in instalments, alleging that he was unable to raise funds and representing that he was insolvent; that such offer contained a specific provision that—

* * * the taxpayer hereby expressly waives—

* * * * *

2. The benefit of any statute of limitations affecting the collection of the liability sought to be compromised, and in the event of the rejection of the offer, expressly consents to the extension of any statute of limitations affecting the collection of the liability sought to be compromised by the period of time (not to exceed two years) elapsed between the date of the filing of this offer and the date on which final action thereon is taken.

that the offer was rejected by the Commissioner by letter dated October 18, 1932; that under date of July 5, 1933,

the plaintiff executed a Tax Collection Waiver which provided as follows: [8]

It is hereby agreed by and between E. C. Simmons of Los Angeles, party of the first part, and the Commissioner of Internal Revenue, party of the second part, that the amount of \$3,472.06, representing an assessment of Income tax for the year 1925 made against the said party of the first part, appearing on the Nov. 590046-1929 assessment list, page....., line, for the Sixth District of California, may be collected (together with such interest, penalties or other additions as are provided for by law) from said party of the first part by distraint or by a proceeding in court begun at any time.

that the Waiver was executed by the Commissioner under date of March 15, 1934; that on May 21, 1936, the plaintiff filed another offer in compromise on Form 656 with the Collector of Internal Revenue at Los Angeles, alleging inability to pay; that this second offer shows as the "Total amount" \$2,316.88, but that it is in reality an offer of \$100, since the offer shows the amount of \$2,316.88 as consisting of \$100 in cash and \$2,216.88 previously paid on account of the tax liability; that this offer contains the specific provision that—

* * * the proponent hereby expressly waives:
* * * * *

2. The benefit of any statute of limitations applicable to the assessment and/or collection of the liability sought to be compromised, and agrees to the suspension of the running of the statutory period of limitations on assessment and/or collection for the period during which this offer is pending and for one year thereafter.

that this offer was rejected by letter dated August 9, 1938; that the plaintiff has never given any notice to the Commissioner that the plaintiff would treat the Tax Collection Waiver as at an end after a reasonable time or at any other time, and that the Tax Collection Waiver remains in full force and effect, and that the collection of the tax in question was not barred when such tax was collected from the plaintiff.

VIII.

Admits the allegations contained in Paragraph VIII of the complaint; denies the allegations contained in the claim for refund except as similar [9] allegations are admitted in this answer.

IX.

Admits the allegations contained in Paragraph IX of the complaint.

Wherefore, defendant prays that plaintiff take nothing by his complaint herein, and that the same be dismissed and that defendant recover his costs in this behalf expended.

JAMES M. CARTER

United States Attorney

E. H. MITCHELL and

GEORGE M. BRYANT

Assistant U. S. Attorneys

EUGENE HARPOLE, Special Attorney,

Bureau of Internal Revenue

By George M. Bryant

Attorneys for Defendant [10]

[Affidavit of Service by Mail.]

[Endorsed]: Filed Aug. 27, 1946. Edmund L. Smith,
Clerk. [11]

[Title of District Court and Cause]

STIPULATION OF FACTS

It Is Hereby Stipulated and Agreed by and between the parties to the above-entitled action, acting through their respective attorneys, that the following facts are true:

I.

This action involves an alleged overpayment of Federal income taxes for the calendar year 1925.

II.

The plaintiff is an individual residing at Beverly Hills, California, and the defendant is and has been since prior to November 14, 1945, the duly appointed and Acting Collector of Internal Revenue of the United States for the Sixth District of California.

III.

On or about June 5, 1929, plaintiff executed an "Agreement as to Final Determination of Tax Liability" fixing the amounts of his income tax liability with respect to the years 1925, 1926 and 1927, which [12] agreement was subsequently approved and accepted by the Commissioner of Internal Revenue.

IV.

On or about October 19, 1929, pursuant to the above "Agreement as to Final Determination of Tax Liability," there were assessed against the plaintiff income taxes for the year 1925 in the amount of \$5,281.66, together with interest thereon in the amount of \$1,053.36, a total of \$6,335.02, against which were credited overassessments for the years 1926 and 1927 in the amounts of \$795.45 and \$2,067.51 respectively, leaving a balance due of \$3,472.06. The Commissioner of Internal Revenue sent

the assessment list containing the foregoing assessment to the Collector of Internal Revenue for the First District of Texas and such Collector received said list on or about November 1, 1929. The foregoing Collector issued against plaintiff a first notice and demand on November 4, 1929, and a second notice and demand with respect to the foregoing liabilities on November 18, 1929. Due to the plaintiff's removal from the First District of Texas to the Sixth District of California, the account for the above income tax liabilities was transferred from the Collector for the First District of Texas to the Collector of Internal Revenue for the Sixth District of California. The Collector for the district last mentioned issued a warrant of distraint with respect to the above liabilities on December 17, 1929, and on December 19, 1929, such Collector filed with the Recorder of Los Angeles County, California, a notice of lien with respect to plaintiff's above income tax liabilities.

V.

From October 19, 1929 to and including August 15, 1933, plaintiff made certain payments on said outstanding balance, which reduced said balance of \$3,472.06 to a balance as of August 15, 1933 of \$1,255.18, exclusive of and not counting interest accruing subsequent to the above assessment on or about October 19, 1929. [13]

VI.

On August 1, 1932, plaintiff executed an "Offer in Compromise" on Treasury Department Form 656 and this offer was filed with the Collector of Internal Revenue at Los Angeles, California, on August 15, 1932. The above Form 656 is a form with printed matter on both the face and the reverse side thereof. Attached hereto

and incorporated herein by reference, is a photostatic copy of the face of the above Form 656, which has been marked Exhibit A-1. Said Exhibit shows that it was executed by plaintiff on August 1, 1932, and that on August 25, 1932 the Commissioner of Internal Revenue, by his duly authorized agent, signed on the face of the above offer with respect to the following language appearing thereon: "Waiver of Statute of Limitations is hereby accepted, and Offer will be considered and acted upon in due course."

VII.

Attached hereto and incorporated herein by reference is a photostatic copy of the reverse side of the above Form 656, which has been marked Exhibit A-2. Said exhibit represents the Collector's recommendation and report to the Commissioner of Internal Revenue as of August 25, 1932, respecting the offer set forth on Exhibit A-1. Exhibit A-2 was executed by the Collector of Internal Revenue for the Sixth District of California on August 25, 1932, and then transmitted to the Commissioner of Internal Revenue in due course.

VIII.

Attached hereto and incorporated herein by reference is a photostatic copy of plaintiff's July 20, 1932 letter to the Commissioner of Internal Revenue, which has been marked Exhibit A-3. Attached hereto and incorporated herein by reference is a photostatic copy of a statement of assets and liabilities which plaintiff submitted with his above letter of July 20, 1932. The foregoing statement has been marked Exhibit A-4. Plaintiff attached Exhibit A-3 and Exhibit A-4 to his above August 1, 1932 Offer in Compromise when he submitted the same to the Commissioner of Internal Revenue. [14]

IX.

On October 18, 1932, the Commissioner of Internal Revenue wrote the plaintiff rejecting the above Offer in Compromise. Attached hereto, incorporated herein by reference and marked Exhibit B is a copy of the Commissioner's October 18, 1932 letter of rejection to the plaintiff.

X.

Between the above date of October 18, 1932, and the hereinafter mentioned date of May 6, 1936, there was no Offer in Compromise pending before the Bureau of Internal Revenue with respect to the above income tax liabilities. On July 5, 1933, plaintiff executed a tax collection waiver with respect to his above income tax liabilities for the year 1925 and on March 5, 1934, the Commissioner of Internal Revenue, by his duly authorized agent, accepted the said waiver executed by plaintiff on July 5, 1933. This waiver was not submitted in connection with any Offer in Compromise. Attached hereto, incorporated herein by reference and marked Exhibit C is a photostatic copy of the above tax collection waiver showing execution thereof by the plaintiff on July 5, 1933 and execution thereof by the Commissioner of Internal Revenue on March 5, 1934.

XI.

On May 6, 1936, plaintiff executed an Offer in Compromise on Treasury Department Form 656 and this offer was filed with the Collector of Internal Revenue at Los Angeles, California, on May 21, 1936. The above Form 656 is a form with printed matter on both the face and the reverse side thereof. Attached hereto and incorporated herein by reference is a photostatic copy of the face of the above Form 656, which has been marked

Exhibit D-1. Said exhibit shows that it was executed by plaintiff on May 6, 1936, and that on May 29, 1936, the Commissioner of Internal Revenue, by his duly authorized agent, signed on the face of the above offer with respect to the following language appearing thereon: "Waiver of statutory period of limitations is hereby accepted, and offer will be considered and [15] acted upon in due course."

XII.

Attached hereto and incorporated herein by reference is a photostatic copy of the reverse side of the above Form 656, which has been marked Exhibit D-2. Said Exhibit represents the Collector's recommendation and report to the Commissioner of Internal Revenue as of May 29, 1936, respecting the offer set forth on Exhibit D-1. Exhibit D-2 was executed by the Collector of Internal Revenue for the Sixth District of California on May 29, 1936; and then transmitted to the Commissioner of Internal Revenue in due course.

XIII.

Attached hereto and incorporated herein by reference is a photostatic copy of "Statement of 1925 income tax of E. C. Simmons" which has been marked Exhibit D-3. Attached hereto and incorporated herein by reference is a photostatic copy of a "Financial Statement of E. C. Simmons," which has been marked Exhibit D-4. Exhibits D-3 and D-4 were prepared by plaintiff and submitted by him in connection with his above Offer in Compromise executed on May 6, 1936.

XIV.

Attached hereto and incorporated herein by reference is a photostatic copy of the copy of the "Tax Collection Waiver" executed by plaintiff on July 5, 1933, which

photostatic copy has been marked Exhibit D-5. The above Exhibit D-2 reads in part as follows: "Were any collection waivers filed? . . . Yes . . . If so, furnish copies . . . attached . . .". Exhibit D-5 represents the collection waiver referred to in the above answer of "Yes" and such exhibit represents the copy of a collection waiver, which the Collector of Internal Revenue for the Sixth District of California "attached" when forwarding to the Commissioner of Internal Revenue (see Exhibit D-2) plaintiff's offer in Compromise executed on May 6, 1936, (see Exhibit D-1). Exhibit D-5 is a copy of plaintiff's original "Tax Collection Waiver" which he executed on July 5, 1933. (See Exhibit C hereto.) [16]

XV.

Attached hereto, marked Exhibit E and incorporated herein by reference, is a copy of the August 9, 1938 letter from the Acting Commissioner of Internal Revenue to the plaintiff whereby the Government rejected plaintiff's above Offer in Compromise executed on May 6, 1936. Plaintiff submitted no further Offers in Compromise and subsequent to the date of August 9, 1938, no Offer in Compromise from the plaintiff was pending or under consideration by the Bureau of Internal Revenue.

XVI.

On or about October 9, 1945, one of the Deputies from the Office of the Collector of Internal Revenue for the Sixth District of California personally called upon and made a demand of plaintiff with respect to the income tax liabilities hereinbefore mentioned. The plaintiff on November 14, 1945, paid to the defendant herein the above balance of \$1,255.18 (see paragraph V hereof) together with interest in the amount of \$1,904.09, or a total of \$3,159.27. In addition to the figure last mentioned plaintiff paid the sum of fifty cents as the fee for obtaining

the release with respect to the lien, which had been created as set forth in paragraph IV hereof.

XVII.

No notice with respect to revoking the above "Tax Collection Waiver" executed by plaintiff on July 5, 1933, and accepted by the Commissioner of Internal Revenue on March 5, 1934, was given unless plaintiff's above offer in compromise executed on May 6, 1936, and filed with the Collector of Internal Revenue on May 21, 1936, constituted such notice.

XVIII.

~~Either party hereto may at the time of trial or writing briefs herein or any other time question the relevancy and/or materiality of any of the facts or exhibits herein stipulated. It is further agreed that this stipulation of facts shall not prejudice the right of either [17] party hereto to introduce such other and additional evidence as is not inconsistent with or contrary to the facts herein stipulated. [LPO H.C.D.]~~

Dated this 5th day of February, 1947.

LATHAM & WATKINS

By Henry C. Diehl

Attorneys for Plaintiff

JAMES M. CARTER

United States Attorney

E. H. MITCHELL and

GEORGE M. BRYANT

Asst. United States Attorneys

EUGENE HARPOLE and

LOREN P. OAKES

Special Attorneys

Bureau of Internal Revenue

By Loren P. Oakes

Attorneys for Defendant [18]

EXHIBIT A-1

Form 656—Revised March, 1929

Treasury Department

Internal Revenue Service

OFFER IN COMPROMISE

To be filed with collector for your district

Forms to be submitted in duplicate

For Use of Collector

Class of tax Income.

Special deposit

account No. 14624.

Serial No. 217.

Amount paid, \$25—

(Cashier's stamp)

Certified Check. Cash. M. O.

E. C. Simmons

(Name of taxpayer)

848 S. Oxford, Los Angeles, California

(Address of taxpayer)

Date—July 20, 1932

Commissioner of Internal Revenue:

Through the Collector of Internal Revenue at Los Angeles, Cal.

Sir:

The following offer in compromise is submitted to you by the undersigned:

Charges of ~~violation of law or~~ failure to meet an internal revenue obligation have been made against the tax-

payer named above as follows: failure to pay I. T. for 1925 amount of \$1330.18 and interest.

(State specifically the pending charge and/or kind of tax and period involved)

Received in

Sep. 3, 1932

General Counsel's Office

Bureau of Internal Revenue

ADMC

Received With Remittance

6th District of California

Aug. 15, 1932

Los Angeles Office

O. G. S.

Date and place of alleged violation.....

The alleged violation or failure is due to the following cause or causes: inability to raise sufficient funds with
(State in detail)

which to make payment.

\$25 paid herewith and balance \$25 monthly.

The sum of \$250.00 is hereby tendered voluntarily with request that it be accepted as a compromise offer and that release be granted the undersigned from the following liability resulting from the violation or failure specified: 1925 income tax in amount of \$1330.18 with accrued interest.

The following facts and reasons are submitted as grounds for acceptance of the offer: insolvent, see statement attached.

(If space provided is insufficient, attach supplemental affidavit and supporting evidence)

It is understood that this *offer* does not afford relief from the liability incurred unless and until it is actually accepted by the Commissioner with the advice and consent of the Secretary of the Treasury, and for cases in suit with the recommendation of the Attorney General of the United States, costs, if any, to be paid by the undersigned.

In making this offer, and as a part of the consideration thereof, the taxpayer hereby expressly agrees that all payments and other credits heretofore made to the account(s) for the year(s) under consideration, for which an unpaid liability exists, shall be retained by the United States, and, in addition, the taxpayer hereby expressly waives—

1. Any and all claims to refunds or overpayments to which he may be entitled under the internal revenue laws for any years, calendar or fiscal, or any period fixed by law, expiring prior to the date of acceptance of the offer, due through overpayment of any tax, interest, or penalty, or interest on overpayments or otherwise, as is not in excess of the difference between the tax liability sought to be compromised herewith and the amount herein offered, and agrees that the United States may retain such refunds or overpayments, if any.

2. The benefit of any statute of limitations affecting the collection of the liability sought to be compromised, and in the event of the rejection of the offer, expressly consents to the extension of any statute of limitations affecting the collection of the liability sought to be compromised by the period of time (not to exceed two years)

elapsed between the date of the filing of this offer and the date on which final action thereon is taken.

(If offer is made by agent, the reason therefor
must be stated on this line)

E. C. Simmons

(Signature of taxpayer or agent)

Sworn and subscribed before me this 1st day of Aug.,
1932.

B. E. Northing

(Signature of officer administering oath)

Waiver of statute of limitations is hereby accepted, and
offer will be considered and acted upon in due course.

Commissioner of Internal Revenue

By.....

Chief Office Deputy

Collector of Internal Revenue [19]

EXHIBIT A-2

COLLECTOR'S RECOMMENDATION

Commissioner of Internal Revenue, Washington, D. C.:

Herewith is an offer made by E. C. Simmons, 848 South Oxford St., Los Angeles, Cal. in compromise of liability incurred because Inability to make further payments on 1925 income tax liability.

Return was filed on Form.....for 1925 on.....
(Period) (Date)

This case is (not) in suit. Tax assessed in Commissioner in First District of Texas.

Record of Assessments and Payments

Entries in detail to be made by the Collector. Show in the tenth column by symbols "Pd.," "Ab.," or "Cr.," the nature of each entry in eighth column.

Kind of Assessment, Tax, Penalty, Interest and Taxable Year	List	Year	Month	Account No. or Page Line	Amount Assessed
Inc Tax	1929	1925	Nov	590046	5281 66
Int to 7/12/29		"	"	"	1053 36
					<hr/> 6335 02
Paid, Abated or Credited				Balance Due	Pd. } Schedule Ab. } Number Cr. }
<u>Date</u>	<u>Amount</u>				
10/31/29	2862 96				Credit 1st Texas
1/ 3/30	241 88				Paid
8/29/30	250 00				"
3/19/31	250 00				"
4/19/31	250 00				"
6/23/31	250 00				"
8/20/31	150 00				"
9/22/31	150 00				"
10/20/31	150 00				"
11/23/31	150 00				"
12/20/31	150 00				"
1/20/32	150 00				"
	5004 84			1330 18	

[STAMPED]:

THIS FORM 656
FOR MEMORANDUM PURPOSES ONLY
OFFER REJECTED 10-18-32
REJECTION SCHEDULE (DATE) 10-27-32

Compromise Offer

Amount of previous tender (\$25.00 herewith)

Balance \$25.00 monthly.

Amount of this tender Tentative..... \$250.00

Total amount offered 250.00

Demands Issued

Form 7658 Date 11/ 4/29 1st Texas

7659 11/18/29 " "

69 12/17/29 6th Calif.

Was a notice of lien filed? Yes 6th District of California
Los Angeles County Dec. 19, 1929.

(If so, when and where)

Was a bond for collection filed? No.

(If so, furnish copy of same)

Was a collection waiver filed? No.

(If so, furnish copy of same)

I recommend that the offer be.....for the
(Accepted or rejected)

following reasons (state same in full):

Being investigated under the provisions of mimeograph
#3832.

Date signed....., 19.....

Collector 6th District of California. [20]

EXHIBIT A-3

Los Angeles, California,
July 20, 1932.

Taxpayer:

E. C. Simmons
808 S. Oxford
Los Angeles, Cal.

Commissioner of Internal Revenue
Through Collector of Internal
Revenue at Los Angeles

Sir:

In connection with attached offer of compromise there is submitted for your consideration:

Additional tax of \$3472.06 became payable at time when my cash position made it impossible to make payment in lump sum. Under an installment arrangement I have paid a total of \$2141.88, leaving a balance, as of July 8, of \$2143.42, interest amounting to \$813.24, and tax of \$1330.18. The last payment, of \$150.00, was made on January 20, 1932. Since that time my financial condition steadily has grown worse, due to successive cuts of salary.

As financial editor of Los Angeles Evening Herald and Express I receive \$180 weekly, my sole income. From this I pay \$216 monthly to an assistant and \$100 monthly to my mother on an old indebtedness. Apartment rent,

household expenses, apparel, doctors and other necessary family expenses aggregate \$385 a month.

In order to hold my position it is necessary that I maintain a standard of living far beyond what otherwise would be justified by my income. I must keep in touch with important people, on a fairly equal footing and do a minimum amount of entertaining, at whatever sacrifice, since my present employment is the direct result of contacts made with my employers before financial troubles multiplied; and I feel quite sure my term would be short indeed once it were known that I am actually bankrupt.

My life insurance premiums average \$250 monthly. These I have managed to keep up by exhausting the loan value of the policies, which will be in default before the end of the current year—something of a calamity since I have lately been pronounced uninsurable.

Prior to the depression I was engaged in the stock brokerage business in Los Angeles. I was caught in the crash. Value of my holdings diminished. I hung on, hoping for a turn of the tide, until I had neither business nor securities.

On page following appears statement of assets and liabilities as of above date, showing an excess of liabilities over assets of \$32,283.35½.

E. C. Simmons [21]

EXHIBIT A-4

ASSETS

	Cost	Current Value
500 shares Builders' Incorporated Mortgages aggregating more than \$60,000 and taxes of more than \$6,000 in default.	\$ 50,000.00	nil
5000 shares of Exchange Publishing Co. Corporation inactive; assets nil unsatisfied judgments outstanding for some \$290.	50,000.00	nil
50 shares Nash-El Paso Motors, Inc. Company inactive with no assets	5,000.00	nil
125 White Sewing Machine notes, no market	468.75	nil
1000 shares Mosqueteros Mining Co., no market	460.00	nil
100 Bach Aircraft. Company out of business	112.50	
1 share Rio Grande Oil Co.	36.50	\$ 2.37½
Membership L. A. Curb Exchange, no market	100.00	nil
Cash	197.00	197.00
	<hr/>	<hr/>
	\$106,374.75	\$199.37½

LIABILITIES

Notes Payable—

Exchange Publishing Co.	\$ 8,707.73
-------------------------	-------------

Mrs. N. C. Simmons	
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(Approx.)	2,000.00
-----------	----------

Repurchase Contract—

Builders Inc. (Approx.)	21,000.00
-------------------------	-----------

Miscellaneous bills past due	775.00
------------------------------	--------

	\$ 32,482.73
--	--------------

Excess of liabilities over	
----------------------------	--

assets	\$ 32,283.35½
--------	---------------

The above in addition to Federal income tax, principal and interest as of July 8, 1932 of \$2143.42. [22]

EXHIBIT B

GC:Adm:C:EMH

260894

Oct. 18, 1932

Mr. E. C. Simmons,
848 South Oxford Avenue,
Los Angeles, California.

Sir:

Careful consideration has been given to the tentative offer of \$250.00 submitted by you in compromise of outstanding balance of income tax for the year 1925, plus assessed interest, in the total amount of \$1,330.18, plus accrued interest, and your offer is hereby rejected as the evidence in the file does not indicate that you are insolvent or unable to pay the full amount of the tax.

You should promptly take up the matter of settlement of this liability with the Collector of Internal Revenue at Los Angeles, California, who is charged with responsibility for collection and is being notified of the rejection of your offer.

Respectfully,

(Signed) David Burnet
David Burnet
Commissioner

- 1 cc Collector, Los Angeles, Calif.
- 3 cc Clearing Division, Comp. Subsec.
- 1 cc A. & C. Unit
- 1 cc I.R.A. in Chge., Los Angeles, Calif. [23]

EXHIBIT C

TAX COLLECTION WAIVER

July 5, 1933

It is hereby agreed by and between E. C. Simmons of Los Angeles, party of the first part, and the Commissioner of Internal Revenue, party of the second part, that the amount of \$3472.06, representing an assessment of income (kind of tax) tax for the year(s) 1925 made against the said party of the first part, appearing on the Nov. 590046-1929 list assessment list, page....., line....., for the Sixth District of California, may be collected (together with such interest, penalties or other additions as are provided for by law) from said party of the first part by distraint or by a proceeding in court begun at any time.

Edward C. Simmons

(Taxpayer)

By.....

Guy T. Helvering

Commissioner of Internal Revenue
Chief Office Deputy

3/5/34 By E. M. Cohee

Collector of Internal Revenue
E.M.C.

If this waiver is executed on behalf of a corporation, it must be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition to which, the seal, if any, of the corporation must be affixed. [24]

EXHIBIT D-1

Form 1656
Treasury Department
Internal Revenue Service
Revised 1934

OFFER IN COMPROMISE

To be filed in duplicate with collector for
your district

For Use of Collector
Class of tax Income
Special deposit
 account No. 891385
Serial No. 54
Amount paid, \$100.00
 (Cashier's stamp)
Certified Check. Cash. M.O.

E. C. Simmons
 (Name of taxpayer)
523 West Sixth St., Los Angeles, Cal.
 (Address of taxpayer)

Date—April 23, 1936

Commissioner of Internal Revenue:

Through the Collector of Internal Revenue at Los
Angeles

Sir:

The following offer in compromise is submitted to you
by the undersigned:

Charges of violation of law or failure to meet an in-
ternal revenue obligation have been made against the pro-

ponent as follows: Failure to pay in full additional 1925 income tax, payable 11/1/29 following ruling that tax accrued in 1925 instead of 1925 and 1926.

(State specifically the pending charge and/or
kind of tax and period involved)

Date and place of alleged violation November 1, 1929
—El Paso, Texas.

The alleged violation or failure is due to the following
cause or causes: Inability to pay owing to lack of funds.

(State in detail)

To secure the release of the proponent from the liability
resulting from the violation or failure above specified, the
sum of \$2,316.88 is hereby tendered voluntarily with re-
quest that it be accepted in compromise of the said liabil-
ity, to wit: tax and interest as per attached schedule,
\$2,216.88 of which already has been paid, as per schedule,
and check is enclosed for remaining \$100. Since it has
been necessary for me to borrow the \$100, its return is
requested in event this offer fails to meet the approval
of the commissioner.

(The liability includes tax or other principal liability,
interest, and/or ad valorem penalty; therefore the *total*
liability for each period involved, for which compromise is
sought, should be stated.)

The following facts and reasons are submitted as
grounds for acceptance of this offer: I am now and have
been for the last several years without regular income and
have subsisted upon borrowed money largely. My liabili-

ties, principally demand notes, exceed \$28,000 with practically no offsetting assets.

(If space provided is insufficient, attach supplemental affidavit and supporting evidence)

It is understood that this offer does not afford relief from the liability sought to be compromised unless and until it is actually accepted by the Commissioner, with the advice and consent of the Secretary of the Treasury.

In making this offer, and as a part consideration thereof, the proponent hereby expressly agrees that all payments and other credits heretofore made to the account(s) for the period(s) under consideration shall be retained by the United States, and, in addition, the proponent hereby expressly waives:

1. Any and all claims to amounts of money to which the proponent may be entitled under the internal revenue laws for any years, calendar or fiscal, or for any period fixed by law, expiring prior to the date of acceptance of this offer, due through over-payment of any tax or other liability, including interest and/or ad valorem penalty, or interest on overpayments, or otherwise, as is not in excess of the difference between the liability sought to be compromised hereby and the amount herein offered, and agrees that the United States may retain such amounts of money, if any.

2. The benefit of any statute of limitations applicable to the assessment and/or collection of the liability sought to be compromised, and agrees to the suspension of the running of the statutory period of limitations on assess-

ment and/or collection for the period during which this offer is pending and for one year thereafter.

(If offer is made by agent, the reason therefor must be stated on this line)

E. C. Simmons

(Signature of proponent or agent)

(Address of agent)

Sworn to and subscribed before me this 6 day of ~~Apr.~~ May, 1936.

James G. Lytho, D.C.

(Signature of officer administering oath)

Waiver of statutory period of limitations is hereby accepted, and offer will be considered and acted upon in due course.

Guy T. Helvering

Commissioner of Internal Revenue

May 29 1936

By E. M. Cohee [Stamped]: Chief Office Deputy
E.M.C. Collector of Internal Revenue

[Stamped]: Received Jul 1, 1936. Technical Staff.

[Stamped]: Received Records Division, Bankruptcy Unit. Jun. 19, 1936. Sub Section G.

[Stamped]: Collr. Int. Rev. 6th California. May 21, 1936. Paid.

[Stamped]: Posting. May 22, 1936. Date. [25]

EXHIBIT D-2

DATA AND RECOMMENDATION SUBMITTED
BY THE COLLECTOR

Commissioner of Internal Revenue, Washington, D. C.:

On reverse side hereof is an offer made by E. C. Simmons, 523 West Sixth St., Los Angeles, Calif., in compromise of liability incurred because Inability to pay additional 1925 tax and interest.

Return was filed on Form.....for.....
(Period)

on.....
(Date)

This case is (not) in suit.

Record of Assessments and Payments

Entries in detail should be made in the appropriate columns below. The next to the last column should show by symbols "Pd.," "Ab.," or "Cr.," the nature of each entry in the preceding column and the last column should show the balance due. All questions below should be fully answered.

Kind of Assessment, Tax, Penalty, Interest and Taxable Year	List	Year	Month	Account No. or Page Line	Amount Assessed
Inc. Tax	1929	1925	Nov.	590046	3285.76
Paid, Abated or Credited				Pd. } Ab. } Cr. }	Schedule No. Balance Due
<u>Date</u>	<u>Amount</u>				
1/·3/30	241.88			Pd.	
8/29/30	250.00			"	
3/19/31	250.00			"	
4/19/31	250.00			"	
6/23/31	250.00			"	
8/20/31	150.00			"	
9/22/31	150.00			"	
10/20/31	150.00			"	
11/23/31	150.00			"	
12/20/31	150.00			"	
1/20/32	150.00			"	
8/15/33	75.00			"	
6/11/34	1255.18			Abt. Uncol	7249.

[STAMPED]:

THIS FORM 656

FOR MEMORANDUM PURPOSES ONLY

OFFER REJECTED 8-9-38

REJECTION SCHEDULE (DATE) 8-12-38

Compromise Offer

Amount of previous tender.....	\$.....
Amount of this tender.....Paid	\$100.00
	<hr/>
Total amount offered..... “	100.00

Demands Issued

Form 69 Date Dec. 17, 1929

Form..... Date.....

Form..... Date.....

Notice of lien was filed on the 20 day of Dec., 1929 at
Los Angeles, Calif.

Was a bond for collection filed?.....

If so, furnish copy of same.....

Were any collection waivers filed? Yes

If so, furnish copies attached

Was the Revenue Agent in Charge requested to make an
investigation? Yes If so, when? 5/19/36.

I recommend* that the offer be.....

(Accepted or rejected)

for the following reasons:

Being investigated under the provisions of Mim.
#3832.

Date signed May 29, 1936.

Nat Rogan

Collector 6th District of California

*Recommendation should always be made if report of
deputy collector is forwarded with this form; if not, the
collector's recommendation should be submitted with the
report of the deputy collector. [26]

EXHIBIT D-3

STATEMENT OF 1925 INCOME TAX
OF E. C. SIMMONSTransferred to Sixth California District From Texas
November, 1929Attached to and made a part of Offer in Compromise
Dated April 23, 1936

Transferred to 6th Cal. for Collection:		\$3472.06
Paid 12/31/29	\$241.88 Treas. Ck.	
9/12/30	250.00	
3/19/31	250.00	
4/19/31	250.00	
6/23/31	250.00	
8/20/31	150.00	
9/22/31	150.00	
10/20/31	150.00	
11/21/31	150.00	
12/20/31	150.00	
1/20/32	150.00	
8/15/33	75.00	2216.88
		<hr/>
Bal. of tax		1255.18
Accrued interest from 11/1/29 to 4/10/36		1341.42
		<hr/>
Total tax and Int. to Apr. 10/36		\$2596.60
		[27]

EXHIBIT D-4

FINANCIAL STATEMENT OF
E. C. SIMMONS523 West Sixth Street
Los Angeles, Calif.

As of April 30, 1936

Submitted to Commissioner of Internal Revenue through
Collector of Internal Revenue at Los Angeles, California,
in connection with Offer in Compromise hereto attached.

Assets:

Miscellaneous items	\$ 1008.17
---------------------	------------

Liabilities:

Demand notes payable	\$23525.18	
U. S. Treasury a/c Income tax	2596.60	
Simmons & Peckham	2084.74	
Misc. personal accounts	1500.00	
	<hr/>	29706.52
Liabilities in excess of assets		\$28698.35

E. C. Simmons

Signature of proponent

Sworn to and subscribed before me this 6 day of
May, 1936.

James G. Lytho, D.C.

Signature of officer administering oath [28]

EXHIBIT D-5

COPY

TAX COLLECTION WAIVER

July 5, 1933

It is hereby agreed by and between E. C. Simmons of Los Angeles, party of the first part, and the Commissioner of Internal Revenue, party of the second part, that the amount of \$3472.06, representing an assessment of Income tax for the year 1925 made against the said party of the first part, appearing on the Nov. 590046—1929 list assessment list, page..... line....., for the Sixth District of California, may be collected (together with such interest, penalties or other additions as are provided for by law) from said party of the first part by distraint or by a proceeding in court begun at any time.

(Sgd.) Edward C. Simmons

“ Guy T. Helvering

Commissioner of Internal Revenue

3/15/34 By E. M. Cohee

Chief Office Deputy [29]

EXHIBIT E

C-TS:PL

CAD:ORM

Aug. 9, 1938

Mr. E. C. Simmons,
523 West 6th Street,
Los Angeles, California.

Sir :

Reference is made to your offer of \$2,316.88, consisting of \$100.00 cash and \$2,216.88 previously paid on

account of your tax liability, submitted through the office of the collector of internal revenue, to compromise your unpaid income tax liability, including interest, for the year 1925.

The tax liability sought to be compromised was made the subject of a final closing agreement entered into by and between you and the Commissioner of Internal Revenue under Section 606 of the Revenue Act of 1928 which was approved on schedule 3159. Accordingly, the tax is legally due.

Careful consideration has been given to the above offer and it is hereby rejected for the reason that the tax is legally due and an amount in excess of the offer appears collectible. There is no authority in the law for the acceptance of an offer in compromise of tax legally due for an amount less than can be collected.

It is suggested that you promptly take up the matter of payment of this liability with the Collector of Internal Revenue, Los Angeles, California, who is charged with the responsibility of collection and is being notified of the rejection.

Respectfully,

Commissioner

1 cc Collector, Los Angeles, Calif.
1 cc I.R.A. in Chg., Los Angeles, Calif.
1 cc Accounts and Collections Unit.
1 cc Records Division.
2 cc Clearing Division, Comp. Subsec.
ORM:NM

[Endorsed]: Filed Feb. 6, 1947. Edmund L. Smith,
Clerk. [30]

[Title of District Court and Cause]

STIPULATION

It Is Hereby Stipulated and Agreed by and between the parties to the above entitled action, acting through their respective attorneys, that the Stipulation of Facts filed herein on February 6, 1947, be amended by striking therefrom paragraph XVIII of the above Stipulation of Facts.

Dated: This 10th day of February, 1947.

LATHAM & WATKINS

By Henry C. Diehl

Attorneys for Plaintiff

JAMES M. CARTER

United States Attorney

E. H. MITCHELL and

GEORGE M. BRYANT

Assistant United States Attorneys

EUGENE HARPOLE and

LOREN P. OAKES

Special Attorneys, Bureau of
Internal Revenue

By Eugene Harpole

Attorneys for Defendant

It Is So Ordered this 11 day of February, 1947.

JACOB WEINBERGER

District Judge

[Endorsed]: Filed Feb. 11, 1947. Edmund L. Smith,
Clerk. [31]

[Title of District Court and Cause]

OPINION

The jurisdiction of this court is invoked pursuant to Section 24 (20) of the Judicial Code as amended (28 USCA Sec. 41 (20)) for the recovery of Federal income taxes which plaintiff alleges were erroneously and illegally collected from him for the calendar year 1925 together with interest in the total amount of \$3,159.27.

Stipulations of facts were entered into between the parties; the case was tried on such stipulations and the testimony of the plaintiff. Briefs have been filed, and the case submitted for decision. We are indebted to counsel for their industrious presentation of the points of law involved herein. Our independent research has disclosed no authority of importance other than that included in their exhaustive briefs and written argument.

The uncontroverted and pertinent facts, as disclosed by the stipulations, exhibits attached thereto, and testimony are as follows:

The taxes herein involved are conceded by the parties to have been properly assessed. [32]

As of November 4, 1929, the balance due was the sum of \$3,472.06. After notice and demand the Collector issued a warrant of distraint on December 17, 1929, and filed a notice of lien on December 19, 1929.

From December 31, 1929 to August 15, 1933, plaintiff made payments in sums varying between \$75.00 and \$250.00, totalling \$2216.88. The balance of \$1255.18, plus interest, is the amount in controversy.

On August 1, 1932, plaintiff executed an "Offer in Compromise" on Treasury Department form 656, and

this offer was filed with the Collector of Internal Revenue at Los Angeles, California, on August 15, 1932. Such printed form included a waiver of the benefit of any statute of limitations affecting the collection of the liability sought to be compromised and consented to the extension of any statute of limitations affecting the collection of the liability by the period of time (not to exceed two years) elapsed between the date of filing said offer and the date on which final action should be taken thereon. Attached to said offer was a letter from the taxpayer to which we shall hereinafter refer, a financial statement of the taxpayer, and the Collector's Recommendation.

The waiver was filed at the request of the Collector of Internal Revenue, and was accepted in writing by the Commissioner; the offer was rejected on October 18, 1932.

On July 5, 1933, plaintiff executed a tax collection waiver wherein the taxpayer agreed that the tax might be collected by distraint or by a proceeding in court "begun at any time." Such waiver was filed at the [33] request of the Collector of Internal Revenue and was accepted in writing by the Commissioner; it was not filed in connection with any offer of compromise, and no compromise offer was pending on July 5, 1933. We shall hereinafter refer to this waiver as the second or unlimited waiver.

On May 6, 1936, plaintiff executed an "Offer in Compromise" on Treasury Department Form 656, and this offer was filed with the Collector of Internal Revenue at Los Angeles, California, on May 21, 1936. Such printed form included a waiver of the benefit of any statute of limitations affecting the collection of the liability sought to be compromised and consented to the suspension of the running of the statutory period of limitations on

collection for the period during which the offer might be pending and for one year thereafter. Attached to said offer was a financial statement signed by the taxpayer under oath. The waiver, to which we shall hereinafter refer as the third or limited waiver, was filed at the request of the Collector of Internal Revenue, and was accepted in writing by the Commissioner. The offer was rejected August 9, 1938.

At the time the last mentioned offer was forwarded to the Commissioner by the Collector, the latter attached to it a copy of the second or unlimited waiver hereinbefore mentioned.

Subsequent to August 9, 1938, no offer in compromise from the plaintiff was pending or under consideration by the Bureau of Internal Revenue, and from that date until October 9, 1945, plaintiff had no correspondence or conferences with the government concerning the tax [34] involved herein, and to plaintiff's knowledge no attempts were made during said period to collect said tax.

On October 9, 1945, the Collector made demand upon the plaintiff for payment of the tax liability involved herein, and on November 14, 1945, taxpayer paid said liability, together with a fee of fifty cents for the release of the lien created as heretofore mentioned.

A claim for refund of the amount paid was filed, and after more than six months during which no action was taken by the Collector with respect to said claim, this action was brought.

The parties have agreed that the only issue before the court is whether the collection of the tax was barred by the statute of limitations, and that the answer to this question depends upon the effect of the second and third waivers given by the taxpayer.

Plaintiff points out in his opening brief that if no waivers had been executed, collection of the tax would have been barred six years after assessment, or on October 19, 1935; that the first waiver extended this period for two months and three days, or until December 22, 1935; that if the second waiver had not been executed, collection would have been barred on December 22, 1935; that the third waiver, (assuming the second to have been effective until the filing of the third) extended the statutory period for collection by three years, two months and nineteen days, or until March 13, 1939; that in order for the defendant to prevail, the second waiver must be held to have been effective not only for the period from December 22, 1935 to May 21, 1936, but also from March 13, 1939 until November 14, 1945, the latter period amounting [35] to nearly seven years.

Plaintiff advances three reasons why the second or unlimited waiver was not in force at the time the tax was collected:

1. The said waiver was invalid from the start and the statute of limitations expired in 1935.
2. The said waiver was good only for a reasonable time, which had expired long before collection in 1945.
3. The third or limited waiver superseded the second or unlimited waiver and established a period of time which expired in 1939.

Plaintiff devotes little argument to his contention that the unlimited waiver was invalid from the beginning, his theory in this regard being that because Section 276 (c), 26 USCA, provides that the tax must be collected within six years after it is assessed or prior to the expiration of

any period for collection agreed upon, a definite period must be stated in a collection waiver, and that the language of the unlimited waiver involved herein did not come within the provisions of the statute. He cites as authority Bouvier's definition of "period" and also quotes the definition of the word as given by Funk and Wagnalls Practical Standard Dictionary.

Defendant replies to this contention with the statement that plaintiff has conceded that Section 276 (c), 26 USCA, applies only to taxable years beginning after December 31, 1938, and that the taxable year 1925 is governed by Section 278 (d) of the Revenue Act of 1924. Defendant further points out that at the time the waiver was executed, there was no statute in effect providing in [36] what manner, or for what period the statute of limitations for collection of taxes might be waived.

Defendant cites Cunningham Sheep & Land Co. (1927), 7 BTA 652, wherein the Board ruled:

(p. 655)

"The position of counsel is that the consent of September 1, 1923, is indefinite in time and is therefore of no effect under the Act, which, it is said by counsel, contemplated an intention that the consent should contain a statement of a 'particular period' during which the assessment might be made. In our opinion the Act does not have the effect of making void such consents as we are here considering. While a consent fixing a definite date for the expiration of the period in which assessment might be made may be desirable to remove uncertainty, there is nothing in the statute which requires that the expiration of the period be related to a definite date."

Plaintiff cites no reported case holding an unlimited waiver invalid because no definite period is fixed, and we find no portion of the statutes cited by either party in their respective briefs which we deem effective to make void the second or unlimited waiver we [37] are here considering.

We shall consider next plaintiff's contention that the third or limited waiver superseded the second or unlimited waiver and established a period of time which expired in 1939.

Plaintiff proposes a rule of construction, "It is a well settled principle of income tax law that doubts as to a waiver's effectiveness must be resolved against the government." In support, he cites two Board of Tax Appeals cases,—*D. J. Gay v. Commissioner*, 31 BTA 580 and *Union Shipbuilding Co. v. Commissioner*, 43 BTA 1143. Both of these cases deal with the authority of a person to execute a waiver on behalf of a dissolved corporation. Those cases, and the cases cited therein, offer no parallel to the matter before us and are of no assistance in determining the issues here raised.

Defendant argues against the principle offered by plaintiff, and cites *Clifton Mfg. Co. v. U. S.*, 3 FS 508, and *W. P. Brown & Sons Lumber Co. v. Commissioner*, 38 F. (2d) 425, as authority that statutes imposing limitations upon action by the United States are to be construed in favor of the government. This principle is enunciated in *E. I. DuPont de Nemours & Co. v. Davis*, 264 US 456, and in *U. S. v. Whited & Wheless, Ltd.*, 246 US 552, while in *United States v. Updike*, 281 US 489, we find the rule given "which requires taxing acts, including provisions of limitations embodied therein, to

be construed liberally in favor of the taxpayer." (P. 496.)

In *United States v. Havner*, 101 F. (2d) 161, Judge Sanborn of the Eighth Circuit observed, when discussing Section 276 (c), 26 USCA: [38]

(p. 165)

" . . . since there is no ambiguity in the language of the section with which we are concerned, there is no room for construction."

We find no ambiguity in the Section above mentioned, and see no necessity for construction.

Plaintiff calls attention to the fact that when the Commissioner accepted the third waiver, he had knowledge that the second, or unlimited waiver, was already on file. This may be assumed, because on Exhibit D-2, it is noted by the Collector that other waivers had been filed, and a copy of the second or unlimited waiver was attached to the offer in compromise which accompanied the second waiver in the Commissioner's file. Plaintiff argues that, when, notwithstanding his knowledge that there was an unlimited waiver on file, the Commissioner accepted the third, or limited, waiver, the Commissioner intended the third or limited waiver to supersede the second or unlimited waiver. Plaintiff cites *Atlantic Mills of Rhode Island v. U. S.*, 3 FS 699 (1933), with the statement that a waiver is not effective until signed by the Commissioner. This question is not before us, as all the waivers herein involved were signed by the Commissioner.

Plaintiff next cites *Helvering v. Ethel D. Co.*, 70 F. (2d) 761 (1934), a case decided by the Court of Appeals of the District of Columbia, upon a Petition of the Com-

missioner for review of a decision of the [39] Board of Tax Appeals. A deficiency had been determined against a corporation, but the tax had not been assessed, when an unlimited waiver was filed. The Board found as a fact that a second waiver was requested immediately upon receipt of the first, and the Board also found that both the taxpayer and the Commissioner intended that the second, or limited, waiver should abrogate the first or unlimited waiver. The Court in its opinion stated:

(p. 762)

"The point in the case is confined to the single issue whether the Board was correct in holding that the making and acceptance of the second waiver abrogated the first. The answer, as we think, depends upon the intention of the parties at the time of the event in question."

The Court then proceeded to review the evidence to ascertain if the same sustained the findings that the second waiver was requested immediately upon receipt of the first and was intended to be substituted for the first.

The Court agreed that the first mentioned finding was sustained by the evidence introduced regarding the dates of the waivers and the correspondence intervening between such dates.

In considering the evidence which justified the finding on intent, the Court stressed these facts:

The second, or limited, waiver was requested immediately after receipt of the first, and enclosed a form of waiver different than the first. [40]

The taxpayer executed the waiver, and at the same time called attention to the fact that it had already executed a different one.

The Court found:

(p. 763)

“The answer of the taxpayer is consistent with the finding of the Board that in signing the second waiver it acquiesced in the request of the Commissioner because it understood the first was not satisfactory and that the second was intended to replace it.”

As further bearing upon the intention of the parties, the Court mentioned that a few months preceding the correspondence the Commissioner had by a departmental ruling limited all unlimited waivers then on file to a definite date and that thereafter it had been the practice of the Bureau in the request for waivers from taxpayers to limit the time of the waiver to the period of one year. Also, a new form of waiver was adopted and substituted for the old form. The unlimited waiver first signed by the taxpayer was on an old and obsolete form. In addition the Court stated:

(p. 763)

“There was doubt whether it was not terminable by the taxpayer on notice, and likewise doubt whether it would terminate without notice after a reasonable time, and it [41] referred to statutes some of which had been repealed. It may very well be, as the Board found, that these reasons impelled the request for the second waiver, and that they likewise indicate the purpose of the parties in executing it, and in this view we should have to affirm the Board’s decision.”

The Court continued:

“But in addition to what has just been said, it is fair to point out that, without regard to the motive

inducing the request for the second waiver, it is undeniable that, when it was returned by the taxpayer and received by the Commissioner, the first waiver had been received and filed. If the Commissioner was satisfied that it conformed to the requirements of the law and rules in relation to waivers and that it was effective to extend indefinitely the time of making the assessment, it was obvious that the second waiver added nothing to what the government already had. Notwithstanding this, the evidence shows the second waiver was accepted and agreed to by the Commissioner. [42] The Board has found as a fact that in this respect the Commissioner intended that it should be substituted for the unlimited waiver, and, since both waivers covered the same subject matter but were inconsistent with one another in relation to the time element, the rule with relation to agreements between the same parties concerning the same subject matter is applicable. In such circumstances, it has invariably been decided that the later rather than the earlier writing will be held to be the agreement between the parties on the subject."

.

(p. 764)

"Nor can there be any doubt of the inconsistency of the two waivers. The first was unlimited. The second required the government to make the assessment prior to the end of the calendar year in which it was executed. In such circumstances it has [43] been held that the provisions of the first clearly inconsistent with the provisions of the later one will be superseded, the inconsistent provisions of the first yielding to those of the second."

In the concluding paragraph of its opinion, the Court cited *Greylock Mills v. Commissioner*, 31 F. (2d) 655, 658, and observed that while it need not decide the question of whether a waiver would fall of itself after a reasonable time, it was admitted that the taxpayer should have the right to terminate such a waiver by notice.

(p. 764)

“ . . . we regard the case here as involving only a question of fact, which, in turn, has been definitely found by the Board against the Commissioner, and which we find there is evidence to sustain.”

Plaintiff also cites *Farmers Union State Exchange v. Commissioner*, 30 BTA 1051. There the statute began to run on June 16, 1919; on January 15, 1923, the taxpayer executed an unlimited waiver; then on June 9, 1924, the taxpayer executed a limited waiver. The Board announced the rule that “An unlimited waiver does not suspend the running of the statute forever, but only for a reasonable time or until the termination by either party upon reasonable notice.” The Board held that under the [44] circumstances, to hold that the first waiver was still in effect after the execution of the second waiver would be the equivalent of “brushing aside” the meaning of the second waiver. In addition, the Board pointed out that the execution of the second waiver, before the first had become effective, was sufficient to constitute a reasonable notice that the first waiver was terminated.

Plaintiff in his reply brief stresses the contention that if the government had no intention that the limited waiver should supersede the unlimited waiver its act of accepting the latter waiver was meaningless. Plaintiff cites *Stange v. U. S.*, 282 U. S. 270, and quotes Judge Brandeis’ con-

cluding sentence in his opinion in this case—(p. 277)—
“It must be assumed that an effective and not a futile act
was intended.”

On the question of whether the limited or third waiver superseded the second or unlimited waiver, defendant Collector cites *U. S. v. Fischer* (1937), 93 F. (2d) 488, a decision of the Second Circuit reversing the District Court's opinion reported at 16 F. S. 743.

In the *Fischer* case, according to the District Court's opinion, the taxes involved were those for the years 1920 and 1921. March 12 and 15, 1926, assessments were made. March 28, 1926, the Collector made demand upon defendant for payment. In its opinion the District Court stated that March 12 and 15, 1932 were the last respective dates for the commencement of actions to collect said taxes. On January 16, 1932, defendant submitted an offer in compromise wherein he consented to the extension of the statute of limitations by the period of time not to exceed two years, elapsed between the filing [45] of the offer and the date on which the final action should be taken. The District Court stated:

(p. 744)

“The effect of this waiver was to interpose a suspension of the statute which on January 16, 1932 would have become operative after the lapse of 56 and 59 days, respectively and those periods were available to the government after action had been taken upon the compromise offer, if the legal situation was unaffected by other events.”

Continuing its summary of the facts, the District Court observed that on February 4, 1932, the taxpayer signed a waiver wherein it was agreed that one tax item might

be collected by distraint or by a proceeding begun at any time prior to December 31, 1933, and on February 5, 1932, a similar waiver was executed with reference to the remaining item. The District Court stated:

(p. 745)

"Standing alone, these papers would seem to limit the government's right to bring suit to December 30, 1933.

"They must have been so construed by the Collector of Internal Revenue, for on September 15, 1933, he wrote to [46] secure additional waivers which would extend the time until December 31, 1934, but none were granted by the administrator.

"The question is whether these two last-mentioned waivers had any effect upon the government's time to bring suit, which 17 days earlier had been enlarged (there being then 56 and 59 days remaining as has been said) by an indefinite period which would not exceed a duration of two years.

"It is interesting to consider why the waivers second in point of time were entered into at all. If they must be now disregarded as having had no necessary place in the relations between the government and the taxpayer, the infirmity was congenital. If that is true, why should the effort have been made to prolong the suspension of the statute by supplementing those waivers for an additional year, as was unsuccessfully attempted on September 15, 1933?

"It will be seen that the government had left less than [47] two months in which to institute suit, when the compromise offer and the waiver accompanying it of January 16, 1932, were filed. If that

offer had been declined by February 2, 1932, suit would have been necessary prior to April 1st of that year. But, by arranging on February 4th for an extension of almost 23 months, the government was sure of that period of time within which it could reject the compromise and bring suit as well. In other words, an indefinite period was exchanged for a definite period, which may have been advantageous to the government from the standpoint of administering the Income Tax Law."

The Circuit Court, in its opinion reversing the District Court mentioned that the lower court had come to the conclusion that the suit was barred, and stated:

(p. 489)

"We think that in so doing an erroneous conception of the effect of the first waiver was entertained. The defendant obtained consideration of his compromise offer by agreeing that the statute of limitations should be [48] extended as therein provided. This effectively tolled the statute for the period up to final action on the offer with a two year limitation. It was not a contract. *Aiken v. Burnet*, 282 U. S. 277, 51 S. Ct. 148, 75 L. Ed. 339. It was but a voluntary unilateral waiver of a defense. *Stange v. U. S.*, 282 U. S. 270, 276, 51 S. Ct. 145, 147, 75 L. Ed. 335. Nor were the subsequent waivers to December 31, 1933 contracts. The extension already in effect was, consequently, not reduced by additional unilateral waivers, since the government relinquished no rights by accepting them. As final action on the offer of compromise was not taken until after the fixed date of the additional waivers had passed, the

parties were simply left as they would have been had they not been executed at all.”

In *Atlantic Mills of Rhode Island v. United States*, 3 F. S. 699, cert. den. 291 U. S. 676, a case cited by plaintiff on a different point, we note the Court looked [49] to the language of a limited waiver to see whether or not by its terms it could be effective as a notice of termination of an unlimited waiver. The limited waiver was not accepted by the Commissioner, but taxpayer contended that, nevertheless, it operated as a notice. A portion of the opinion of the Court of Claims reads:

(p. 703)

“The document relied upon by plaintiff in support of these contentions, executed on February 9, 1923, is not susceptible of the construction that it was a notice to the Commissioner that the waivers theretofore duly executed and filed with the Commissioner and approved and signed by him February 9, 1923, would terminate on December 31, 1923.

“By its plain terms this document was clearly intended as a consent in writing by the taxpayer and the Commissioner with respect to 1917, and it was executed and filed with the Commissioner with that purpose in mind and with the view that it would be approved and signed by the Commissioner as a waiver contemplated by the statute rather than as a notice that the con- [50] sents theretofore filed and approved would terminate and become ineffective after December 31, 1923. The language of the document shows that it was intended as a waiver rather than as a notice”

There is nothing in the language of the third or limited waiver which could lead us to believe that it was intended as a notice of termination of the unlimited waiver. Nor are we required, if such were not the purpose of the third or limited waiver, "to brush aside the meaning of the later waiver" within the language of *Farmers Union State Exchange v. Commissioner*, 30 B. T. A. 1051; nor, are we required, if such were not the purpose of said waiver, to assume that by requesting such waiver, a futile act was intended to be accomplished. On the contrary, it is logical to assume that when the Commissioner requested the third waiver, he intended to secure a fixed period within which he might consider the compromise offer and investigate the financial status of the taxpayer, during which period, in the event the taxpayer filed notice of termination of the unlimited waiver, the Commissioner would not be left without a waiver.

We therefore hold that the second or unlimited waiver was not terminated by the giving of the third or limited waiver.

Plaintiff further maintains that a waiver which is not limited as to duration is valid only for a reasonable time, and calls attention to the fact that the elapsed [51] time from the date of filing of the second or unlimited waiver to the date of collection of the tax amounts to twelve years, four months and nine days during the last seven years, three months and five days of which time there were no proceedings of any sort had or pending between the plaintiff and the government; that more than a reasonable length of time had elapsed and the waiver was therefore no longer in effect at the time collection was made.

In support of such theory, plaintiff cites *Herman Frost v. Commissioner*, 23 B. T.A. 411, decided in 1931, and

Nathan Loeser v. Commissioner, 27 B. T. A. 601, decided in 1933.

In the Frost case, the member rendering the opinion [LBF 3/3/48] had stated that the Board ~~that~~ theretofore held that where a waiver was filed which provided for determination, assessment and collection irrespective of any period of limitations, the Commissioner had a reasonable time within which to act. (Citing: Cunningham Sheep & Land Co., 7 B. T. A. 652; Greylock Mills, 9 B. T. A. 1281, aff'd. 31 F. (2d) 655; William S. Doig, Inc., 13 B. T. A. 256; and Corn Products Refining Co., 22 B. T. A. 605.) It was further mentioned that a claim for abatement had been filed, and that a very confused state of affairs existed with reference to the liability of the parties concerned on account of the dissolution of the corporation. The deficiencies were assessed in January 1924, the waiver filed in 1924, and petitioner was advised of his liability in January 1927. The Board held that "in view of the record" the lapsed time was not unreasonable and that collection was not barred by the statute.

In the Nathan Loeser case (*supra*), the member who [52] rendered the opinion stated therein:

(p. 604)

"We have frequently held that an unlimited waiver permits the Commissioner a reasonable time in which to act. Cunningham Sheep & Land Co., 7 BTA 652; Greylock Mills, 9 BTA 1281; aff'd. 31 Fed. (2d) 655, Cert. den. 280 US 566; William S. Doig, Inc., 13 BTA 256; Herman Frost, 23 BTA 411.

"What is a reasonable time is not to be determined abstractly or solely by reference to the calendar. It

depends on all the circumambient facts of the situation. . . . In the instant case, judged solely by the calendar, a very considerable time elapsed between the signing of the waiver and the issuance of the notice of deficiency. But, viewed in the light of all the facts, each being related directly or indirectly to the other, we do not believe it can properly be said that respondent failed to act within a reasonable time . . . [53]

“The waiver in question was requested, executed and received only because of the controversy relating to the taxable status of the corporation. It specifically refers to the matter as did the forwarding letter. The action of both the petitioner and the corporation in filing claims for refund shows that they were continuously aware of the uncertainty of the outcome and sought to protect themselves by filing such claims. In order to avoid a multiplicity of proceedings the respondent refrained from taking action as to the 1920 tax until the identical issue should be decided by the Board. Under such circumstances, we are of the opinion that the respondent acted within a reasonable time.”

The Nathan Loeser case, as the Frost case, previously hereinabove mentioned, involved the determination of a liability. The waiver was dated September 25, 1925. The notice of deficiency was issued July 17, 1931.

It is interesting to note that both the Frost and the Loeser opinions include in their citations of [54] authorities on the point that an unlimited waiver permits the Commissioner a reasonable time to act, the case of Greylock Mills, 9 B. T. A. 1281, *aff'd.* 31 Fed. (2d) 655.

In *Cunningham Sheep & Land Company*, 7 B. T. A. 652, we find an expression of the reasoning upon which the Board based its "reasonable time" theory:

(p. 655)

"The courts are frequently confronted with contracts which fail to fix the period within which they are to be performed. Courts are reluctant to declare any contract void for uncertainty if the intent of the parties can be determined. In those cases where the uncertainty relates to the time of performance of the contract, the courts have found little difficulty in arriving at the conclusion that a reasonable time is to be allowed. There are some variations of this rule, one of which permits one of the parties in certain circumstances to give notice to the other of the time within which performance should be made, reasonable notice being given. It appears to us that the rules laid down by the courts for construction of such agreements are [55] properly to be applied to the consent entered into between the Commissioner and this taxpayer and that under the consent of September 1, 1923, the Commissioner was given a reasonable time after the date of its execution in which to determine and assess the deficiency."

The defendant Collector disagrees with plaintiff's contention that the waiver fell after the lapse of a reasonable time, and cites *Greylock Mills v. Commissioner*, (C. C. A. 2, 1929), 31 F. (2d) 655, Cert. Den. 280 U. S. 566.

The *Greylock* case concerned the statute of limitations with reference to the assessment of a deficiency and the Board of Tax Appeals held that the Commissioner acted

within [LBF 3/3/48]

~~with~~ a reasonable time after the execution of an unlimited waiver, a period of three years having elapsed.

The Circuit Court affirmed the Board of Tax Appeals decision, (31 F. (2d) 655), stating that it might rest its affirmance upon the same ground as that of the Board, that the Commissioner acted within a reasonable time. At page 658:

“But there is also another ground equally fatal to appellant’s contention. If waivers which are in terms unlimited are to be limited at all, we think they should expire only after the taxpayer gives notice to [56] the Commissioner that he will regard the waiver as at an end after a reasonable time, say three or four months, from the date of such notice. In such a rule there is no harshness to either party; on the contrary, it seems to us the most reasonable one. An analogy may perhaps be found in the case of contracts for the sale of land, where time does not ordinarily become of the essence unless expressly so stated, until notice is given by one party and an opportunity afforded to the other to act. (citing cases.) In the instant case, no such notice was given to the Commissioner, and we think the waiver remained outstanding so that he was entitled to act at his leisure.”

In *Greylock Mills v. White*, 63 F. (2d) 866, the First Circuit in its opinion at page 868 stated:

“The waiver in this case, being unlimited in duration extended the period for the assessment and collection of the 1918 tax at least a reasonable time beyond the then statutory limit of June 15, 1924.

(citing cases.) Whether it [57] continued the period indefinitely until either the taxpayer or the commissioner gave notice of the termination of the waiver, it is not necessary to decide, although it might be so terminated at any time on reasonable notice given by either."

At page 868, the First Circuit commented upon the opinion of the Second Circuit heretofore mentioned and reported at 32 F. (2d), 655:

"The Circuit Court of Appeals held that the waiver in this case was effective in extending the time for both assessment and collection of the 1918 tax beyond the limitation fixed in the prior statutes, and expressed the opinion that it extended the time for collection of a tax assessed prior to the date of its execution and until the taxpayer gave notice of a termination of the waiver. On the last proposition we express no opinion."

Defendant Collector also cites *Big Four Oil & Gas Co. v. Heiner*, 57 F. (2d) 29 (1932), a decision of the Third Circuit Court of Appeals, wherein there was a delay of four and a half years between assessment and collection of deficiency income tax because of taxpayer's claim for [58] credit. The Court stated:

(p. 30)

"The only question, therefore, to be decided is whether or not the unlimited waiver filed March 2, 1923, authorized the collection by distraint in November, 1928 of the tax assessed on March 15, 1924.

"If such a waiver does require the Commissioner to act within a reasonable time, the evidence was

sufficient to allow the court below to say that the period between the assessment, March 15, 1924, and the collection of the deficiency, November 8, 1928, was not unreasonable, because shortly after the assessment the appellant filed a claim for credit which was duly considered and rejected prior to June 24, 1927, when the second notice and demand were issued. . . . The delay in collecting the tax must have been caused by the time required to consider the appellant's claim for credit. It cannot object to a delay that it caused."

The Circuit Court then cited the case of *Greylock Mills v. Lucas*, 31 F. (2d) 655, and quoted from [59] the portion of the opinion in that case wherein it was held that an unlimited waiver remains outstanding until notice is given of its termination. After such quotation, the Court in the *Big Four Oil & Gas Co. v. Heiner* case said:

(p. 31)

"This rule seems reasonable and the present case falls within its scope."

In *Warner Sugar Refining Company*, 4 B. T. A. 5, the Board considered an unlimited waiver, stating:

(p. 11)

"No notice was ever served upon the Commissioner by the taxpayer prior to the assessment of the amount here in controversy as to when it would regard the provisions of the waiver as having been fully complied with by both parties and become inoperative."

In *F. L. Bateman v. Commissioner*, 34 B. T. A. 351, the Board held:

(p. 358)

“Under all the facts and circumstances here present, the delay in mailing the notice of deficiency, about $4\frac{1}{4}$ years after the expiration of the statutory period for assessment had expired, is not so unreasonable as to invalidate the waiver for [60] 1920.

“Furthermore, it has been held that waivers unlimited as to time expire only upon reasonable notice to that effect given by the taxpayer. (Citing *Greylock Mills v. Commissioner*, 31 F. (2d) 655.) No notice was given here.”

Defendant directs attention to the fact that in none of the Board of Tax Appeals cases cited by plaintiff did the Board conclude the Commissioner had failed to act within a reasonable time, and that therefore it was not, in any of the cases cited, necessary for the Board to pass upon the question whether an unlimited waiver survived beyond a reasonable time and until notice of its revocation was given by the taxpayer. In view of our conclusions hereinafter expressed we, also, find it unnecessary to pass upon that portion of plaintiff's contentions.

The plaintiff points out in his brief that there elapsed a period of seven years between the rejection of the last offer in compromise and the collection of the tax on November 14, 1943:

1945 [LBF 3/3/48]

vember 14, 1943:

“Thus for a period of more than seven years the government chose to remain inactive regarding the collection of these taxes . . . this period of in-

activity is so patently unreasonable that the court should, as a matter of law find that the government failed to act within [61] a reasonable time."

We note that in the letter from the taxpayer which accompanied the first offer in compromise disclosed that the taxpayer held a position, the salary for which, even after successive cuts, amounted to at least \$720.00 a month. In the letter the taxpayer stated that his position was the result of contacts made with his employers before his financial troubles multiplied, and he indicated that were his financial status known his employment would be shortly terminated; he detailed his expenses, and presented the sad picture of a man, formerly affluent, who had been caught in the crash, who had been forced to borrow on his insurance to support his family; that his insurance would shortly be in default, and he had been pronounced uninsurable. His financial statement showed an excess of liabilities over assets of the sum of \$32,-482.73. It was a year after writing this letter, and after he had been informed that the Collector would not accept his offer in compromise, and that he should promptly take up the matter of his liability with the Collector, that the taxpayer executed the second, or unlimited waiver.

We note also that in the offer of compromise filed in 1936, the taxpayer stated he had been without regular income and that he had subsisted largely upon borrowed money; he offered \$100.00 in compromise of his liability, and stated he had been obliged to borrow that sum; his financial statement showed liabilities in excess of assets in the sum of \$28,698.35.

Again, on August 9, 1938, the government rejected his offer in compromise, and again suggested that he

promptly take up the matter of his liability with the [62] Collector of Internal Revenue at Los Angeles.

In *Nathan Loesner v. Commissioner*, 27 B. T. A. 601, cited by plaintiff, it is stated that what constitutes a reasonable time is not to be determined abstractly or solely by reference to the calendar; that it should be viewed in the light of all the facts of the situation. In each of the cases cited by counsel wherein it is considered whether the elapsed time is reasonable, the facts and circumstances are different. None of the cases to which our attention has been directed provide us with a measuring stick for "reasonable time" in the matter before us, because, in most if not all of those cases, the period considered was one during which the Commissioner had failed to assess, or to finally determine after a controversy, the amount owed by the taxpayer. Here the amount had been determined; that it was due had been conceded by the taxpayer. There was no failure of the government to act which was occasioning the taxpayer anxiety, inconvenience, or uncertainty.

We believe that in determining what constitutes a reasonable time in cases such as this, the court should consider not only the facts and circumstances present in each case, but also the objects of statutes of limitations in connection with such particular facts and circumstances.

In *Bell v. Morrison*, 26 U. S. 350, Justice Story commented:

(pp. 360-361)

" . . . It is a wise and beneficial law, not designed merely to raise a presumption of payment of a just debt from lapse of time, but to [63] afford

security against stale demands, after the true state of the transactions may have been forgotten, or be incapable of explanation, by reason of the death or removal of witnesses. It has a manifest tendency to produce speedy settlements of accounts, and to suppress those perjuries which may rise up at a distance of time, and baffle every honest effort to counteract or overcome them. . . . The statute of limitations was not enacted to protect persons from claims fictitious in their origin, but from ancient claims, whether well or ill founded, which may have been discharged, but the evidence of discharge may be lost."

The unlimited waiver provided clearly that the tax might be collected "at any time." There is no doubt that the taxpayer gave such waiver in the hope that the government might refrain from drastic collection procedure which would imperil taxpayer's means of livelihood, and that the taxpayer might be given grace to enable him to pay his debt without the necessity of such procedure.

" . . . definite unambiguous statements in written waivers, [64] made for the purpose of obtaining action favorable to the maker and on which such action is obtained, must be given effect." (S. S.

[LBF 3/3/48] 93

Pierce Co. v. U. S., 935 F. (2d) 599, at 601.)

We assume that the taxpayer, when he gave the unlimited waiver, intended to pay the debt to the government which he conceded to be due. That the government withheld action, over a long period, and made final de-

mand at a time when taxpayer was able to discharge his just liability, should not be deemed unreasonable. As was said in *Shambaugh v. Scofield*, 132 F. (2d) 345,—(p. 347): “Having had full advantage of the waivers, the taxpayers should not now be heard to repudiate them unless they were clearly inoperative.”

For the reasons herein stated, we conclude that at the time of collection of the tax, the second or unlimited waiver was operative.

Dated this 26th day of February, 1948.

JACOB WEINBERGER

United States District Judge

[Endorsed]: Filed Feb. 26, 1948. Edmund L. Smith, Clerk. [65]

[Minutes: Wednesday, March 3, 1948]

Present: The Honorable Jacob Weinberger, District Judge.

It appearing that through inadvertence the opinion filed herein on Feb. 26 1948, contains several typographical errors, it is ordered that said opinion be corrected by the clerk by interlineation as follows: page 21—6th word of line 15 the word “that” should be changed to “had”. Page 25—line 19: the word “with” should be changed to “within”. Page 30—line 24: the figures “1943” should be changed to “1945”. Page 34—line 7: the figures “935” should be changed to “93”. [66]

[Title of District Court and Cause]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above case came on regularly for trial on February 6, 1947, before the above entitled Court sitting without aid or intervention of a jury; the plaintiff appearing by Latham and Watkins by Henry C. Diehl, Esq., and the defendant appearing by James M. Carter, United States Attorney for the Southern District of California; George M. Bryant, Assistant United States Attorney for said District, and Loren P. Oakes, Special Attorney, Bureau of Internal Revenue; and the trial having proceeded and a Stipulation of Facts by the parties hereto having been [67] submitted, and oral evidence on behalf of plaintiff also having been submitted to the Court for consideration and decision, and the Court on the 26th day of February, 1948, having rendered its opinion herein, and the Court from the foregoing Stipulation of Facts and oral evidence, makes the following Findings of Fact and Conclusions of Law:

FINDINGS OF FACT

1.

This action involves an alleged overpayment of Federal income taxes for the calendar year 1925.

2.

The defendant is and has been since prior to November 14, 1945, the duly appointed and acting Collector of Internal Revenue of the United States for the Sixth District of California, and plaintiff is an individual residing within said District.

3.

On or about October 19, 1929, there was assessed against the plaintiff income taxes for the year 1925; certain overassessments for other years were credited against the amount assessed, leaving a balance due of \$3,723.06. Notice and demand were issued on November 4, 1929 and on November 18, 1929; on December 17, 1929, a warrant of distraint was issued with respect to such liability, and on December 19, 1929, notice of lien was filed with the County Recorder of Los Angeles County, California.

4.

Plaintiff made payments from time to time in [68] amounts varying between \$75.00 and \$250.00 on said outstanding balance, until on August 15, 1933, at which time the balance due on said tax was the sum of \$1,255.18, with interest thereon.

5.

On August 1, 1932, plaintiff executed an "Offer in Compromise" on Treasury Department Form 656, a printed form including a waiver with respect to the statute of limitations, which waiver provided that the taxpayer waived the benefit of any statute of limitations affecting the collection of the liability sought to be compromised and in the event of the rejection of the offer expressly consented to the extension of any statute of limitations affecting the liability sought to be compromised by the period of time, not exceeding two years elapsed between the date of the filing of the offer and the date on which final action thereon should be taken. The offer and waiver were executed at the request of the Collector of Internal Revenue, and were filed with the Collector of Internal Revenue at Los Angeles, California, on August 15, 1932.

6.

Plaintiff attached to said "Offer in Compromise" his letter dated July 20, 1932, addressed to the Commissioner of Internal Revenue, wherein the taxpayer enclosed a financial statement which showed liabilities in amount of \$32,482.73 in excess of his assets, and wherein he indicated that should his financial status become known to his employer he would lose his position.

7.

On August 25, 1932, the Commissioner of Internal Revenue accepted in writing said Waiver of Statute of [69] Limitations, and on October 18, 1932, said Commissioner rejected the "Offer in Compromise."

8.

On July 5, 1933, at the request of the Collector of Internal Revenue, the taxpayer executed a "Tax Collection Waiver," wherein it was agreed between the Commissioner of Internal Revenue and the Taxpayer that the amount of \$3,472.06 representing an assessment of income tax for the year 1925 might be collected, together with interest, from the taxpayer by distraint or by a proceeding in court begun at any time.

9.

At the time the waiver last above mentioned was executed no offer in compromise was pending, and the waiver was not submitted in connection with any offer in compromise. Said waiver was accepted in writing by the Commissioner on March 5, 1934.

10.

On May 6, 1936, plaintiff executed an "Offer in Compromise" on Treasury Department Form 656, a printed

form including a waiver with respect to the statute of limitations, which waiver provided that the taxpayer waived the benefit of any statute of limitations affecting the collection of the liability sought to be compromised, and agreed to the suspension of the running of the statutory period of limitations on assessment or collection for the period during which the offer should be pending and for one year thereafter. By said "Offer in Compromise" the taxpayer tendered the sum of One Hundred Dollars in [70] settlement of the balance then due, and stated in said offer that the taxpayer had been without regular income for several years and had subsisted largely upon borrowed money. With said offer, the taxpayer included a financial statement which showed his liabilities in the amount of \$28,698.35 in excess of assets. Said offer and waiver were executed at the request of the Collector of Internal Revenue, and were filed with the Collector of Internal Revenue at Los Angeles, California, on May 21, 1936. The Collector of Internal Revenue at Los Angeles transmitted said offer and waiver to the Commissioner of Internal Revenue, therewith forwarding a copy of the Tax Collection Waiver filed July 5, 1933.

12.

The waiver executed May 6, 1936 was accepted by the Commissioner of Internal Revenue in writing on May 29, 1936, and on August 9, 1938, said last mentioned "Offer in Compromise" was rejected by said Commissioner.

13.

Subsequent to said date of August 9, 1938, no offer in compromise from the plaintiff was pending or under

consideration by the Bureau of Internal Revenue, and subsequent to said last mentioned date and until October 9, 1945, plaintiff had no correspondence or conferences with the Government concerning the taxes herein involved, and to plaintiff's knowledge no attempts were made during said period to collect said taxes.

14.

On October 9, 1945, the Collector of Internal Revenue made demand upon plaintiff for the payment of the [71] balance due on said taxes, and on November 14, 1945, plaintiff paid said balance of \$1,255.18 together with interest amounting to \$1,904.09, together with the sum of fifty cents for the release of the lien created as hereinbefore mentioned. A claim for refund for the amount of said tax and interest so paid was filed by the plaintiff, and after more than six months during which said claim for refund was neither accepted nor rejected, this action was brought.

15.

No notice with respect to revoking the Tax Collection Waiver executed July 5, 1933 was given by plaintiff.

16.

Under all the circumstances herein shown no unreasonable time elapsed prior to the date when the Government collected the taxes herein involved from the plaintiff.

From the foregoing Findings of Fact, the Court draws the following

CONCLUSIONS OF LAW

1.

The Tax Collection Waiver executed by plaintiff on July 5, 1933 was valid.

2.

Said Tax Collection Waiver of July 5, 1933 was not revoked or terminated by the execution and acceptance of the waiver of May 6, 1936. [72]

3.

Said Tax Collection Waiver of July 5, 1933 was not revoked or terminated by the lapse of time herein.

4.

Said Tax Collection Waiver of July 5, 1933 was operative at the time said taxes were collected.

5.

The collection of said taxes was not barred by any statute of limitations.

6.

Plaintiff has not overpaid the taxes and interest involved herein and is entitled to no relief by his said complaint.

7.

Defendant is entitled to judgment herein with costs.

Dated this 23 day of April, 1948.

JACOB WEINBERGER

United States District Judge

[Endorsed]: Filed Apr. 23, 1948. Edmund L. Smith,
Clerk. [73]

In the District Court of the United States
Southern District of California
Central Division
No. 5517-W

E. C. SIMMONS,

Plaintiff,

vs.

HARRY C. WESTOVER, Collector of Internal Revenue,
Defendant.

JUDGMENT

The above case came on regularly for trial on February 6, 1947, before the above entitled Court sitting without aid or intervention of a jury the plaintiff appearing by Latham and Watkins by Henry C. Diehl, Esq., and the defendant appearing by James M. Carter, United States Attorney for the Southern District of California; George M. Bryant, Assistant United States Attorney for said District, and Loren P. Oakes, Special Attorney, Bureau of Internal Revenue; and the trial having proceeded and a Stipulation of Facts by the parties hereto having been submitted, and oral evidence on behalf of plaintiff also having been submitted to the Court for consideration and decision, and the Court after being fully advised in the premises and after due deliberation, having rendered its Opinion herein on February 26, 1948, and having filed its Findings of Fact and Conclusions of Law and ordered that judgment be entered in favor of the defendant in accordance with said Findings and Conclusions; [74]

Now, Therefore, by virtue of the law and by reason of the Findings and other matters aforesaid, it is considered and ordered by the Court that the above entitled action be dismissed and that defendant have judgment for and shall

recover from plaintiff the amount of defendant's costs, to be taxed by the Clerk of this Court in the sum of \$10.00.

Judgment rendered this 26 day of March, 1948.

JACOB WEINBERGER

United States District Judge

Judgment entered Apr. 26, 1948. Docketed Apr. 26, 1948. Book 50, page 403. Edmund L. Smith, Clerk; by L. B. Figg, Deputy.

Judgment Satisfied 5-18-1948 by flg. satis. Edmund L. Smith, Clerk U. S. District Court, Southern District of California; by Wm. A. White, Deputy. [75]

[Affidavit of Service by Mail.]

[Endorsed]: Filed Apr. 26, 1948. Edmund L. Smith, Clerk. [76]

[Title of District Court and Cause]

NOTICE OF APPEAL

Notice Is Hereby Given that E. C. Simmons, plaintiff above named, hereby appeals to the Circuit Court of Appeals for the Ninth Circuit from the final judgment entered in this action on April 26, 1948.

LATHAM & WATKINS

By Henry C. Diehl

June 21, 1948. [77]

* * * * *

Received copy of the within Notice of Appeal and Appellant's Designation of Record on Appeal this 21 day of June, 1948. James M. Carter, U. S. Atty., by Gertrude M. Johnson, Attorney for Deft.

[Endorsed]: Filed Jun. 21, 1948. Edmund L. Smith, Clerk. [80]

[Title of District Court and Cause]

CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the District Court of the United States for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 81, inclusive, contain full, true and correct copies of Complaint for Refund of Income Taxes Paid; Answer; Stipulation of Facts; Stipulation and Order Amending Stipulation of Facts; Opinion; Minute Order Entered March 3, 1948; Findings of Fact and Conclusions of Law; Judgment; Notice of Appeal and Appellant's and Appellee's Designations of Contents of Record on Appeal which, together with copy of Reporter's Transcript of proceedings on February 6, 1947, transmitted herewith, constitute the record on appeal to the United States Circuit Court of Appeals for the Ninth Circuit.

I further certify that my fees for preparing, comparing, correcting and certifying the foregoing record amount to \$16.50 which sum has been paid to me by appellant.

Witness my hand and the seal of said District Court this 13 day of July, A. D. 1948.

(Seal)

EDMUND L. SMITH

Clerk

By Theodore Hocke

Chief Deputy Clerk

[Title of District Court and Cause]

Honorable Jacob Weinberger, Judge Presiding

REPORTER'S TRANSCRIPT OF PROCEEDINGS

February 6, 1947, Los Angeles, California

Appearances:

For the Plaintiff: Latham & Watkins by Henry C. Diehl, Esq., 1112 Title Guarantee Building, Los Angeles, California.

For the Defendant: Loren Oakes, Special Attorney, Bureau of Internal Revenue; and George M. Bryant, Assistant United States Attorney.

Los Angeles, California, February 6, 1947,
2:00 O'clock P. M.

(Case called by clerk.)

Mr. Diehl: The plaintiff is ready.

Mr. Oakes: The defendant is ready.

Mr. Diehl: If the court please, I think it is advisable that I make a brief opening statement to apprise you of the nature of the action. This case involves the alleged overpayment of 1925 income taxes. The facts are, mostly, undisputed, I believe.

In October, 1929, the tax was duly assessed. There is no argument about that. Thereafter came the crash or that was about the time of the crash, and the plaintiff was unable to pay the amount in full and he made part payments through the years until, in 1935, the amount was reduced to the amount involved in this suit.

On October 15, 1932, the plaintiff filed an offer in compromise, incorporated in which was a waiver of the

statute of limitations for the time which the government would take to consider the offer in compromise.

On October 18, 1932, this offer in compromise was rejected.

Thereafter, on July 5, 1933, the plaintiff executed what is entitled a tax collection waiver, which purports to extend the statute of limitations indefinitely. [2*]

On March 15, 1934, this waiver was executed by the Commissioner.

On May 21, 1936, a second offer in compromise was filed by the taxpayer. This offer also contained a waiver of the statute of limitations for the period during which the offer was pending and for one year thereafter. On August 9, 1938, this was rejected by the Commissioner.

Thereafter, nothing transpired between this taxpayer and the government until October of 1945, when the notice and demand for payment of the tax was presented to the plaintiff. On November 14th, 1945, he paid the tax and, on December 11th, he filed a claim for refund. And, after waiting the six months' period, during which no action was taken, on June 27, 1946, this action was filed.

The only issue is whether or not the collection of tax was barred by the statute of limitations. The plaintiff says it was and the defendant says it was not, and relies upon the collection waiver of July, 1933, which purported to suspend the statute of limitations indefinitely, the so-called unlimited waiver.

Our theory of the case is, one, that an unlimited waiver is good for only a reasonable length of time, in any event, and that the time that has elapsed is much more than a reasonable length of time; two, that that waiver,

*Page number appearing in original Reporter's Transcript.

contained in the second offer in compromise, filed after the so-called unlimited [3] waiver, superseded the so-called unlimited waiver, and the government is bound by the time mentioned in this second offer in compromise.

The Court: Will you repeat that last statement?

Mr. Diehl: That the waiver contained in the second offer in compromise, which was filed in 1936, supersedes the so-called unlimited waiver filed in 1933 and sets a definite time limit in this case, March 13, 1939.

The Court: Is that the one that provides for a year?

Mr. Diehl: Yes; that is, for the period during which the offer was being considered, plus one year. That would bar the taxes as of March 13, 1939. Of course, they were not collected until some six and a half years later.

We have an additional argument, which has apparently never been considered in any court, and that is that an unlimited waiver is not valid in any event for the reason that the taxes shall be collected within six years after assessment or within such period as is agreed upon, in writing, by the Commissioner and the taxpayer. And our argument will be that the word "period" means a definite period and not an unlimited period.

Now, as I say, the facts are, mostly, undisputed. The pleadings contain allegations of fact which are admitted. In addition to that, we have signed a stipulation of facts which contains practically all of the rest of the facts necessary to [4] the case, and I would like to submit the stipulation at this time, duly signed by counsel for both sides.

As far as the plaintiff is concerned, we would like to introduce about 15 minutes of oral testimony by the plaintiff, and that will be our case.

The Court: Isn't that testimony covered in your stipulation of facts?

Mr. Diehl: No; it is not. These are facts which were not such that the government chose to stipulate to them. I don't know whether they will be controverted or not.

Mr. Oakes: If your Honor please, I would like to mention that the statement which has been made by Mr. Diehl represents a pretty good summary of the matters which have gone into this statement of facts. We have tried to make the stipulation run, for the sake of simplicity, in chronological order.

It is true there was an offer made in 1932. This offer, of course, was rejected during that same year and, hence, I don't believe either party hereto or the court will find that that 1932 offer is of any particular relevancy.

However, when we come into the next year, 1933, the taxpayer did execute a waiver, which is attached to the stipulation as Exhibit C, and by its precise terms, it is notice to the government to make an assessment or, rather, to make collection, at any time. The assessment had already been made in [5] 1929, so this waiver was given so that the collection could be made at any time. Now, had that offer not been given in 1933, the time would have expired by the applicable periods of limitation. So the purpose of the waiver was so that the government wouldn't have to harass the taxpayer and he has more time, and, if his financial circumstances change in due course, his tax liability would be ultimately paid off and the Commissioner doesn't have to resort to his drastic remedies of collection, distraint, and so forth. This 1933 unlimited waiver, on which we rely, was signed by the Commissioner in 1934.

The Court: Did that waiver precede the other waiver or follow it?

Mr. Oakes: This particular waiver, then, is sandwiched in between the 1932 offer of compromise and the 1936 offer in compromise.

The Court: And the 1936 offer in compromise limited the consideration within a year after the acceptance or rejection of the offer?

Mr. Oakes: The 1936 offer in compromise was made on a printed form and one of the standard clauses which appeared in print was that the statute of limitations should not run while the offer was under consideration and for one year thereafter.

The Court: And that was rejected?

Mr. Oakes: That was rejected [6]

The Court: You are relying, then, on the unlimited waiver?

Mr. Oakes: Which preceded it in 1933.

The Court: What is your contention as to that waiver?

Mr. Diehl: When we say that the offer of compromise was rejected, we mean the offer in compromise; not the waiver. It is shown on the form there that the waiver was accepted by the Commissioner. In other words, the Commissioner accepts the waiver when the offer in compromise is filed. Then, he later rejected the offer in compromise. But that doesn't mean he rejected the waiver.

Mr. Oakes: As Mr. Diehl says, there is a sentence on the 1936 offer whereby, as an administrative matter, the Commissioner states that he will accept the waiver above set forth and will consider the offer in due course.

Now, on this standard form 656, which was used both in 1932 and also in 1936, the reverse side provides for the Collector reporting to the Commissioner as to the

status of this account and the receipt of this offer, which the Collector must transmit to the commissioner in Washington, D. C. In transmitting this 1936 offer to the Commissioner in Washington, D. C., the Collector is required to report whether there are any waivers on file. By that is meant, obviously, a waiver other than the waiver set forth on the face of the offer. So that the Collector reported to the Commissioner, in 1936 [7] "Here is a 1936 offer in compromise. We forward it to you. We also have a waiver on file." And he forwarded a copy of this unlimited waiver which was executed three years before.

I mention this because the cases lay considerable stress upon the intention of the parties, and at least the intention of the Collector, as the representative of the government, was that in forwarding this 1936 offer the situation was protected by an unlimited waiver which was obtained in 1933, a copy of which was attached to the 1936 offer.

I realize that opposing counsel will advance legal arguments that there might have been a superseding waiver. That is a point which we wish to prove in due course before your Honor.

The Court: This payment was finally made when?

Mr. Oakes: It wasn't made until 1945, and at that time we went out and made a notice and demand and, pursuant to that notice, the taxpayer paid in 1945 what he, obviously couldn't pay in earlier years when he was reporting that he was \$28,000 in the red.

The Court: That waiver that you rely upon was executed when?

Mr. Oakes: In 1933.

The Court: Some 12 years before this?

Mr. Oakes: That is correct.

• The Court: Followed by another waiver and followed by [8] an offer of compromise and an extension of the limitation period at that time?

Mr. Oakes: I think it is worthy of note that this 1933 waiver was given at a time when there wasn't any offer in compromise pending whatsoever. So its purpose was to maintain the status quo. In 1936 that document, according to the government's position, was for the purpose of submitting an offer in compromise and, as an incidental, it did have language suspending the running of the statute of limitations. We think, under the authorities, the government was entitled to the specific revocation of an unlimited waiver and, had there been any such notice, as a matter of practicality, the Commissioner would have protected himself before the expiration of the limitation period.

The Court: Are there any questions arising in relation to such a payment? Of course, it is not an overpayment—

Mr. Oakes: I believe the taxpayer would say it is an overpayment because it is outlawed or barred by the statute and, conversely, we say it isn't because it is not outlawed and not barred by the statute of limitations. The merits of that tax are not in dispute but rather the issue of the statute of limitations.

Mr. Diehl: If I may, I think the answer to your Honor's question is that the Internal Revenue Code defines a payment of taxes, after the statute has expired, as an overpayment on [9] which the taxpayer is entitled to a refund. So, if the statute has expired, it is an overpayment and, if the statute has not expired, it is not an overpayment.

Mr. Oakes: We believe that it would be an overpayment provided, of course, that the court should decide

adversely to the government on the issue of the statute of limitations.

The Court: Now you wish to proceed with the introduction of your testimony?

Mr. Diehl: Yes, sir.

Mr. Oakes: I have just one more remark to make.

The Court: Go ahead.

Mr. Oakes: I don't believe anyone representing the government has heretofore heard any expression of what I must say is a rather novel point by Mr. Diehl, that, because there was an indefinite period prescribed in the 1933 waiver, the 1933 waiver was thereby rendered void. It would be, certainly, diametrically opposed to the intention of the parties, when they have a waiver saying that an assessment can be made at any time, to apply an interpretation which would say it is no good, even for one minute, because it is not definite. The courts have had these unlimited waivers before them and they have been upheld. So the government, of course, is violently opposed to any such radical interpretation of the document as that.

The Court: I imagine you have authorities in connection [10] with your waivers.

Mr. Oakes: Opposing counsel intimated that that point hadn't been heretofore urged. It appears he is more ingenious than any of his predecessors.

The Court: Does a waiver of that kind resemble the waiver in some of these promissory note matters, that are unlimited?

Mr. Oakes: We haven't studied any such analogy but it is a point we would be glad to cover in briefs.

The Court: I don't know whether it is applicable here. You may proceed, then, with the introduction of your testimony.

Mr. Diehl: Mr. Simmons.

E. C. SIMMONS,

the plaintiff, being first duly sworn, testified as follows:

Direct Examination

By Mr. Diehl:

Q. State your name, please.

A. Edward C. Simmons.

Q. You are the plaintiff in this action?

A. I am.

Q. Mr. Simmons, I refer you to Exhibit A-1 attached to the stipulation which is on file herein, which purports to be an offer in compromise, dated July 20, 1932. Do you recall [11] the circumstances under which that offer in compromise was filed? A. I do.

Q. At whose request was that offer filed?

A. At the instance of the Internal Revenue Department.

The Court: Is that Exhibit 1?

Mr. Diehl: That is Exhibit A-1, your Honor.

Q. At the time you executed this offer in compromise, Exhibit A-1, did you know that it included a waiver of the statute of limitations, in definite terms?

A. I did.

Q. Now I refer you to Exhibit C attached to the stipulation, which is a so-called tax collection waiver, dated July 5, 1933. Do you recall the circumstances under which that waiver, Exhibit C, was executed and filed? A. Yes.

The Court: You have asked about A-1. Did you ask about A-3?

Mr. Diehl: I have skipped A-2, -3, -4 and B.

Q. At whose request was the collection waiver, Exhibit C, filed?

(Testimony of E. C. Simmons)

Mr. Oakes: To which the government objects. Here we have a document which speaks for itself. The two parties, the taxpayer and the government, have agreed to this, as indicated by their signatures, and whether the government requested the [12] taxpayer or whether the taxpayer requested the government can't have any legal effect whatsoever or any significance on this document. They arrived at that agreement and, under the parol evidence rule, there is no reason to modify it. And, particularly because of the immateriality and irrelevancy of that question, the government objects, and there is no ambiguity there to be explained.

Mr. Diehl: If the court please, the government did announce the possibility that intent may have a good deal to do with this case, and we believe these questions are material in arriving at that intent. Specifically, we believe it is important to show that the government asked for these waivers, in order to carry forward and show the intent of the taxpayer and the government in subsequent dealings. Moreover, we also have the rule of evidence, set forth by Rule 43(a), that the rules of evidence in the State where the court is sitting are to be recognized and evidence is to be admissible if there is any ground for it. And we think the rule in California that circumstances surrounding the execution of a written instrument make it admissible in evidence is applicable.

The Court: If there is any doubt as to the contents of the instrument.

Mr. Diehl: There is no doubt as to the contents of the instrument. We are merely getting at the surrounding circumstances and showing the intent of the parties in all their [13] dealings.

(Testimony of E. C. Simmons)

Mr. Oakes: For what purpose? How could there be any proof concerning circumstances unless there is something equivocal in this document that needs interpretation? If there were some other construction before the court, it might be necessary to enter into the surrounding circumstances to see. And I believe the document speaks for itself, and I don't believe there is anything to construe.

The Court: Your contention is that here is a document that was executed by the taxpayer and that the question of the intent has some place in the execution of this document?

Mr. Diehl: Not particularly in the execution of this document as particularly in the matter which follows. I believe, if this so-called unlimited waiver was executed at the request of the government and subsequently another document was executed at the request of the government, that that means the second document shall supersede the first.

The Court: Isn't that a question of law?

Mr. Diehl: Frankly, I think it is but the government seems to indicate the intent may have something to do with this. I am merely trying to anticipate some argument which the government will put on probably by briefs.

The Court: If there is some understanding between the parties when the document is executed as to whether they will replace it or supplant it with another document, then I think [14] the surrounding circumstances may be introduced, but here I don't know whether the question of intent has any bearing. The document was executed. And the man who executed it intends to use it, does he not?

Mr. Diehl: Yes, sir.

(Testimony of E. C. Simmons)

The Court: The same as a promissory note or a check. Otherwise, he wouldn't have executed the agreement. If this was executed with some intent that is not disclosed in the document—

Mr. Diehl: As to this particular document, you may be correct.

The Court: I don't know whether it is admissible or not to show intent, that is, intent standing alone and not connected with any other issue. I am inclined to believe that the document speaks for itself and the question of intent is immaterial. The objection is sustained.

Q. By Mr. Diehl: Now, Mr. Simmons, relative to Exhibit D-1 attached to the stipulation of facts, the exhibit immediately following Exhibit C, which we have been talking about—

A. Yes, sir.

Q. —that was an offer in compromise, dated April 23, 1936. Do you recall the circumstances surrounding the filing of this offer?

A. I do.

Q. At whose request was it filed? [15]

Mr. Oakes: The government wishes to make the same objection. We think the analogy here is like a contract. We think it is analogous to a contract because it is signed by the taxpayer and subsequently signed by the Commissioner.

The Court: Would it make any difference at whose request?

Mr. Oakes: That is not material, I don't think.

The Court: I don't see any harm in that question.

Mr. Oakes: I am also trying to anticipate as well as Mr. Diehl. I fear that the taxpayer is going to try and make capital out of whose request this was, and I believe the legal results are the same regardless of who requested it.

(Testimony of E. C. Simmons)

The Court: That is probably true.

Mr. Oakes: And, if that is so and being immaterial, I don't want the record cluttered with it.

The Court: I don't think there is any harm in stating at whose request it was done. He may answer that question.

A. At the instance of someone in the Internal Revenue Department.

Q. By Mr. Diehl: At the time that this so-called second offer in compromise, Exhibit D-1, was filed, did you recall the fact that you had already executed Exhibit C, the tax collection waiver?

A. I did, indeed, and I was firmly of the opinion—

Mr. Oakes: I believe the government should move to [16] strike all of his opinion and recollections.

The Court: It may be stricken.

Q. By Mr. Diehl: At the time the second offer in compromise, Exhibit D-1, was filed, did you know that the government had already on file a so-called unlimited waiver?

A. Yes, and I was firmly of the opinion—

Mr. Oakes: I move to strike, again, his opinion in that regard.

The Court: Just answer the question, and, if your counsel wants to ask you anything else, he will ask it and proper objection may be made then.

Q. By Mr. Diehl: Did you intend that the waiver contained in that second offer in compromise should supersede the previously executed tax waiver?

Mr. Oakes: The government objects because counsel is trying to insert in the record a mere subjective matter of the state of mind of the witness and we can't interpret

(Testimony of E. C. Simmons)

agreements by what was in his mind. And it was never communicated to the government. Therefore, it is immaterial.

The Court: The witness can't answer it. The matter of intent has no bearing on the subject, I don't think. I mean it is his state of mind.

Mr. Diehl: That is quite true. Of course, we believe that the intent is shown in the record.

The Court: Whatever the record shows— [17]

Mr. Diehl: As I say, I am merely anticipating that the government is going to make certain representations and we must show the actual intent of the parties aside from that. If they will stipulate that, I will be glad to withdraw my question.

The Court: If they do, it will have to be construed from the documents, I imagine, unless there is some evidence bearing on the subject.

Mr. Diehl: Then, I take it the objection is sustained, is it?

The Court: The objection is sustained.

Q. By Mr. Diehl: Do you know, Mr. Simmons, what the local Collector's recommendation was with respect to the second offer in compromise, Exhibit D-1?

A. I was informed it had gone forward to Washington with the recommendation that it be accepted.

Q. Now, with reference to Exhibit E, which is the letter from the Commissioner, dated August 9, 1938, rejecting the offer in compromise of April 23, 1936, Exhibit D-1, to the best of your recollection, did you have any correspondence or discussions with the Treasury Department on the subject of these taxes from that date until October of 1945?

A. No.

(Testimony of E. C. Simmons)

The Court: To which exhibit are you referring?

Mr. Diehl: Exhibit E, the last exhibit. [18]

Q. From the date of that letter until the month of October, 1945, were any attempts made to collect these taxes from you?

A. Not that I can recall.

Q. There were, then, no proceedings of any kind, so far as you recall, pending between you and the government from August, 1938, to October, 1945?

A. No, sir.

The Court: What do you mean by "proceedings"?

Mr. Diehl: Well, pending offers in compromise, correspondence or anything relating to these taxes, and no visits from the Collector in attempting to collect. In other words, the matter was completely at rest from August, 1938, to October, 1945.

The Court: Is there any dispute about that?

Mr. Diehl: The stipulation contains only the fact that there were no offers in compromise pending. I merely want to get into the record the fact that there was nothing pending.

Mr. Oakes: The government hereby objects to the question as immaterial. We had an unlimited waiver and we can proceed against the taxpayer whenever we see fit to do so.

The Court: I think he may answer if there was any correspondence took place or any conferences. It will be limited to those matters, correspondence or conferences with any department. [19]

Mr. Diehl: I believe he has answered the question but I will state it again to be sure.

(Testimony of E. C. Simmons)

Q. During the period of August 9, 1938, to October, 1945, did you have any correspondence with the government concerning your 1925 income tax?

A. No, sir.

Mr. Oakes: For the purpose of the record, the government wishes to repeat the same objection, that these conversations are immaterial under our rights under the unlimited waiver.

The Court: That is between what dates?

Mr. Diehl: Between August 9, 1938, and October—, what was the date of that demand, Mr. Oakes? Do you know?

Mr. Oakes: I believe the stipulation says there was a demand in October, 1945. It is paragraph 16 of the stipulation.

Mr. Diehl: Yes, October 9, 1945.

Q. During that period, you had no discussions with any—

The Court: I will rule on that objection. There was an objection made.

Mr. Oakes: Yes, your Honor. I objected to that.

The Court: The objection is overruled.

Q. By Mr. Diehl: Were there any discussions between you and any representative of the government, during that period, regarding your 1925 tax? [20]

Mr. Oakes: The same objection.

A. Not that I can recall.

The Court: Overruled.

Mr. Bryant: Your Honor, the witness answered.

A. Not that I can recall.

(Testimony of E. C. Simmons)

Q. By Mr. Diehl: Were any attempts made to collect the 1925 tax during that period?

Mr. Oakes: The government objects to that as calling for a conclusion of the witness and it would involve matters not within his knowledge, and also the ground of immateriality.

The Court: When you talk about an attempt, that presupposes some act or something of that kind.

Mr. Diehl: I think it is probably covered by the other questions anyway, that he had no correspondence or conferences as far as he knew. I will withdraw that question. You may cross examine.

The Court: I think that question has been formerly asked, the first question; that it was asked when you referred to Exhibit E, and there was no objection at that time whether there was any attempt to collect,—

Mr. Diehl: I believe that is correct.

The Court: —if I am not mistaken.

Mr. Oakes: I don't recall, your Honor.

The Court: I have it in my notes here.

Mr. Oakes: That being the case, for the purpose of the [21] record, I would like to move to strike testimony with respect to attempts to collect on the ground it calls for the conclusion of the witness on matters that took place in government offices, unbeknownst to the taxpayer.

The Court: That motion may be granted. It seems to me that you gentlemen can stipulate, if between these dates there had been any correspondence or there had not been—you might include that in your stipulation, if there was any correspondence, on both sides, and that would simplify the situation from a legal standpoint.

Mr. Oakes: I am not able to state with certainty what actually transpired at that time and I would rather leave the court without anything on that phase.

The Court: Very well. The reason I mentioned that was to see whether it is possible to submit the entire matter on an agreed statement of facts.

Mr. Oakes: I want to confer just a moment, if I may. No cross examination.

Mr. Diehl: The plaintiff rests.

Mr. Oakes: For the purpose of the record, do I understand that the stipulation is now being received for consideration by your Honor?

The Court: I will look at it. Paragraph XVIII. "Either party hereto may at the time of trial or writing briefs herein or any other time question the relevancy and/or [22] materiality of any of the facts or exhibits herein stipulated. It is further agreed that this stipulation of facts shall not prejudice the right of either party hereto to introduce such other and additional evidence as is not inconsistent with or contrary to the facts herein stipulated."

What is your present attitude as to the relevancy or materiality of the facts or exhibits stipulated to under this stipulation?

Mr. Diehl: If the court please—

The Court: I don't want to be put in this position. I don't want to begin the consideration of a case and have someone, at the last moment, in his brief, object to the relevancy and upset perhaps my whole line of thinking on the solution of the case.

Mr. Diehl: Frankly, my feeling is that Exhibits A-1, -2, -3 and -4 and Exhibit B, are probably relevant except

to this extent: I will restrict that as far as A-2, -3, and -4 are relevant. Exhibit A-1 is relevant because it contains a waiver of the statute which it is necessary to use in computing when the collection became barred. Exhibit B is material because it shows the length of time during which this particular offer was being considered and is necessary to a computation of the extension. Exhibit C is, of course, quite material. It is the government's whole case. Exhibit D-1 is also very material because that is our case, or [23] a good part of it. Our claim is that Exhibit D-1 supersedes Exhibit C. D-2 is material, I take it, because of its reference to the preceding waiver. D-3 and D-4, I believe, are not material. D-5, I believe we will both agree, is material, we for one reason and the government for another. Exhibit E is also material in that it shows the length of time during which the offer was being considered. The facts stated in the stipulation—I believe there are some there which are not material and I don't believe they have any bearing on the case one way or the other and that they shouldn't upset anybody. They are just preliminary to what goes on here. The only argument in the case is was the collection barred by the statute of limitations. We admit the taxes were properly assessed.

Mr. Oakes: Your Honor, I believe it would be unwise to strike any paragraph or sentence from the stipulation and, likewise, inadvisable to strike any of these exhibits because they give the continuity and they give the chronological story of what happened, and it wouldn't give your Honor a clear picture of the history if anything were stricken. And as to these offers in compromise, we now give your Honor the picture. When we photostat something, obviously, we have to photostat both sides and,

therefore, get two sheets. Now, just by illustration, A-1 in the original, which I have before me, is just one sheet of matter, written on both sides, [24] and I don't believe that, when we place in evidence an offer in compromise, it would be fair or complete to place in evidence anything less than the entire document.

The Court: Is Exhibit A-2 on the reverse side of Exhibit A-1?

Mr. Oakes: Yes, your Honor.

The Court: Does the stipulation so indicate?

Mr. Oakes: Yes, I think it is fairly clear that took place.

The Court: What is wrong with that?

Mr. Diehl: Not a thing. The fact of the matter is I don't object to the inclusion of any evidence. I think it can all be in there and probably should be to show the whole story.

The Court: You have only one thing in this case, just one issue, the question as to whether or not this agreement can extend the statute indefinitely?

Mr. Diehl: That is right.

The Court: Everything else is merely explanatory, I imagine.

Mr. Diehl: I don't really think your Honor will have any trouble regardless of how much we may say in our briefs about something being irrelevant and immaterial. And I will withdraw my objections.

The Court: You withdraw your objection? [25]

Mr. Diehl: Yes.

The Court: Then may it be understood—or what is the understanding with respect to Paragraph VIII? Shall this matter be submitted to the court, subject to objections to be made later on, or not?

Mr. Bryant: Does your Honor mean Paragraph XVIII?

The Court: Yes; Paragraph XVIII.

Mr. Oakes: If your Honor wants it submitted, I presume both sides could agree that this is all that is going to appear before your Honor. There is no further evidence on either side. The government doesn't have any evidence now and is willing to waive the right to present any further evidence.

The Court: What I referred to is this. While this is a stipulation, yet it isn't, because this paragraph recites that "Either party may, at the time of trial or writing briefs herein or any other time question the relevancy and/or materiality of any of the facts or exhibits herein stipulated." The court is unwilling to accept the conclusion of a trial in that form. That doesn't conclude the trial.

Mr. Diehl: I am perfectly willing to strike that portion of the stipulation.

Mr. Oakes: We will join with opposing counsel in that suggestion.

The Court: Paragraph XVIII may be stricken from the [26] stipulation of facts, may it?

Mr. Diehl: I think the entire paragraph. We have introduced additional evidence and it is in. I think the whole paragraph should be stricken.

The Court: I think this may be done by additional stipulation instead of striking it, without making a physical striking at this time. Or would you prefer to strike it out now by running lines through it?

Mr. Oakes: In the event of possible appeal, it might be simpler to have it stricken, the entire Paragraph XVIII, and we could stipulate the clerk could strike Paragraph XVIII.

Mr. Diehl: That is agreeable.

The Court: It is agreeable to both sides that Paragraph XVIII may be stricken from the stipulation, is that correct?

Mr. Diehl: Yes, that is correct.

Mr. Oakes: That is correct, your Honor.

The Court: It is so ordered. However, that doesn't take with it the striking of the testimony offered by the plaintiff in this case today.

Mr. Oakes: Yes; that is what the government has in mind, that this Paragraph XVIII relates exclusively to the preceding seventeen paragraphs in the stipulation and does not relate to the transcript wherein the taxpayer testified.

The Court: Then, the testimony as submitted today may [27] stand as having been—

Mr. Diehl: Yes; I think there is no difficulty there. It merely states "the following facts are true."

Mr. Oakes: Again for the purposes of the record, the taxpayer's testimony stands subject to the rulings your Honor has made to certain portions?

The Court: Yes. I think we had better cover that with a stipulation, a written stipulation. You can cover that with a written stipulation, can you not?

Mr. Oakes: Yes, your Honor.

The Court: Then, that will be in the file and that will constitute a better record.

Mr. Oakes: I will prepare it and forward it and send a copy to counsel.

The Clerk: I have already stricken it, your Honor.

The Court: You gentlemen may initial this and the record may show that the striking of this paragraph is covered by a written stipulation to be filed.

Mr. Oakes: Does your Honor want the record to show that you are receiving this in evidence or that it is filed?

The Court: This stipulation may be received in evidence. That is agreeable to both sides, is it?

Mr. Diehl: Yes, your Honor.

Mr. Oakes: And I believe the plaintiff has heretofore rested, and, now that the submission is in evidence, the [28] government will accordingly rest. The defendant rests.

The Court: We should have arguments and briefs. I imagine you would like to file written arguments and briefs.

Mr. Diehl: If the court please, I think probably we should confine it to written arguments and briefs and not attempt any oral arguments at this time.

Mr. Oakes: May I suggest, your Honor, I believe the usual practice is that the taxpayer can file an opening brief and we can reply and then he can file a reply brief and, after the issues are somewhat clarified by that process, if your Honor would desire it, then we could come in and discuss it?

Mr. Diehl: That is all right.

The Court: That course may be followed. How long do you want to file your opening brief and argument?

Mr. Diehl: 10 days.

The Court: Do you want longer?

Mr. Diehl: I think I can do it in 10 days.

The Court: All right. And you want 10 days, do you?

Mr. Oakes: Mr. Bryant just reminded me that our docket is a little heavy. Would 20, 20 and 10 be more feasible?

Mr. Diehl: That is all right, your Honor.

The Court: Very well; 20, 20 and 10, will be all right.

The Clerk: That will run into the criminal calendar, your Honor. [29]

Mr. Oakes: Those are the dates on which we will get in those three briefs?

The Court: I couldn't take this matter under submission during the time I have the criminal calendar. I begin that on the 29th of March.

Mr. Oakes: If it is agreeable to Mr. Diehl, any subsequent date after your criminal calendar we will appear for any oral argument.

The Court: I may not require oral arguments.

Mr. Oakes: We can leave that in this way—

The Court: I don't think this is a very complicated situation. It is purely a question of law.

Mr. Diehl: That is correct.

The Court: There are no facts that seem to control the situation other than what you have set out in your stipulation. We can set it down for March 31st for further presentation or arguments and I can continue that until—I have the criminal calendar in April, May and June.

Mr. Diehl: The plaintiff is willing to shorten the period within which to file briefs if that will help the situation.

Mr. Oakes: If it will expedite the matter, your Honor, 15 and 15 and 7 or something like that, which will put us through a lot sooner.

The Court: It won't make any difference to me. [30]

Mr. Oakes: Or two weeks, two weeks and one week. The government does feel that, as this case will require your Honor to interpret unlimited waivers, and the government has had a great many of them decided, there could be an important precedent and possibly it might require a careful presentation. And we would like to

see it set for oral argument as well as thorough briefing, and with that in mind—

The Court: That is right. After you have filed your arguments and briefs, I may want some oral argument following that.

Mr. Oakes: And the government would like to present it also orally at that time as well as giving our views in written form.

The Court: I will be pretty busy with the criminal calendar. So I won't have much time to digest matters. Follow the course that has been outlined, 20, 20 and 10, and we will put it on the calendar for March 31st for oral argument. I think I will have time on that day to take the civil calendar in the afternoon.

Mr. Bryant: Is this matter at 2:00 p. m., your Honor?

The Court: 2:00 p. m., on March 31st. Do you want today's record written up?

Mr. Bryant: Yes, your Honor. That will be requested.

Mr. Diehl: And the plaintiff also.

The Court: And will you see that the court is furnished [31] with a copy?

Mr. Bryant: The government cannot furnish a copy, your Honor. However, there will be one in the clerk's file as long as one is ordered by either party.

The Court: Then the court can resort to the one on file.

(Recess.)

[Endorsed]: Filed Jul. 13, 1948. Edmund L. Smith, Clerk. [32]

[Endorsed]: No. 11973. United States Circuit Court of Appeals for the Ninth Circuit. E. C. Simmons, Appellant, vs. Harry C. Westover, Collector of Internal Revenue, Appellee. Transcript of Record. Upon Appeal From the District Court of the United States for the Southern District of California, Central Division.

Filed July 14, 1948.

PAUL P. O'BRIEN

Clerk of the United States Circuit Court of Appeals for
the Ninth Circuit

In the United States Circuit Court of Appeals
for the Ninth Circuit

Docket No. 11973

E. C. SIMMONS,

Appellant,

vs.

HARRY C. WESTOVER, Collector of Internal Revenue,
Appellee.

STATEMENT OF POINTS AND DESIGNATION
OF PARTS OF RECORD TO BE PRINTED

To the Clerk of the United States Circuit Court of
Appeals for the Ninth Circuit:

I.

STATEMENT OF POINTS

Appellant intends to rely upon the following points:

(1) The District Court erred in entering judgment for the appellee.

(2) The District Court erred in failing to enter judgment for appellant in the amount of \$3,159.27 as prayed for, plus interest and costs of suit.

(3) The District Court erred in failing to find or conclude that appellant had overpaid his federal income taxes and interest thereon for the calendar year 1925 in the amount of \$3,159.27.

(4) The District Court erred in failing to find or conclude that the collection from appellant by appellee of \$3,159.27 in federal income taxes and interest for the calendar year 1925 was, on the date of said collection, to-wit, November 14, 1945, barred by the provisions of Section 276(c) of the Internal Revenue Code (26 U. S. C. A., Section 276(c)).

(5) The District Court erred in failing to find or conclude that the Tax Collection Waiver dated July 5, 1933 (Exhibit C attached to the Stipulation of Facts), was void ab initio.

(6) The District Court erred in failing to find or conclude that said Tax Collection Waiver (Exhibit C), if not void ab initio, was effective for only a reasonable length of time and that the time elapsed from the date thereof until the date of collection of the tax and interest for the calendar year 1925 was more than a reasonable length of time.

(7) The District Court erred in failing to find or conclude that said Tax Collection Waiver (Exhibit C), if not void ab initio, was, in any event, superseded and rendered no longer effective by the provisions of the Offer in Compromise dated April 23, 1936 (Exhibits D-1 and D-2 attached to the Stipulation of Facts).

II.

DESIGNATION OF PARTS OF RECORD TO BE PRINTED

Appellant respectfully submits that all of the record on appeal, as certified to you, will be necessary for the consideration of the points upon which appellant intends to rely. Accordingly, appellant requests you to have printed the entire record on appeal in this case.

LATHAM & WATKINS

By Henry C. Diehl

1112 Title Guarantee Building

Los Angeles 13, California

Attorneys for Appellant

[Affidavit of Service by Mail.]

[Endorsed]: Filed Aug. 2, 1948. Paul P. O'Brien,
Clerk.

No. 11973.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

E. C. SIMMONS,

Appellant,

vs.

HARRY C. WESTOVER, Collector of Internal Revenue,

Appellee.

BRIEF FOR APPELLANT.

LATHAM & WATKINS,

DANA LATHAM,

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1112 Title Guarantee Building, Los Angeles 13,

Attorneys for Appellant.

FILED

OCT - 9 1948

PAUL P. O'BRIEN,



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No. 11973.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

E. C. SIMMONS,

Appellant,

vs.

HARRY C. WESTOVER, Collector of Internal Revenue,

Appellee.

BRIEF FOR APPELLANT.

Jurisdiction.

This appeal involves an alleged overpayment of Federal income taxes for the calendar year 1925. The taxes and interest involved, in the amount of \$3,159.27, were paid to appellee by appellant on November 14, 1945, and a claim for the refund thereof was filed with appellee by appellant on December 11, 1945.

Thereafter, on June 27, 1946, more than six months having elapsed during which time said claim for refund was neither approved nor rejected, the complaint herein [Tr. 2-6] was filed pursuant to section 24(20) of the Judicial Code as amended (28 U. S. C. A., Sec. 41(20)).

The judgment of the District Court of the United States for the Southern District of California, Central

Division, in favor of the appellee, was entered on April 26, 1948 [Tr. 75], and this appeal is taken pursuant to section 128 of the Judicial Code as amended (28 U. S. C. A., Sec. 225). The Notice of Appeal was filed on June 21, 1948 [Tr. 75] pursuant to Rule 73(a) of the Federal Rules of Civil Procedure.

Opinion Below.

The only previous opinion rendered in this cause is the opinion of the District Court [Tr. 41-67] reported in 76 Fed. Supp. 442.

Issues Involved.

Was the collection, on November 14, 1945, by appellee from appellant of \$3,159.27 in Federal income taxes and interest for the calendar year 1925 barred by the statute of limitations on collection with the result that appellant has overpaid his taxes and interest for said year and is entitled to the refund thereof with interest as provided by law.

Statutes Involved.

(1) Section 278 of the Revenue Act of 1926, as amended by the Revenue Act of 1928 (26 U. S. C. A., Internal Revenue Acts, page 209) provides in part as follows:

“(d) Where the assessment of any income, excess-profits, or war-profits taxes imposed by this title or by prior Act of Congress has been made (whether before or after the enactment of this Act) within the period of limitation properly applicable thereto, such

tax may be collected by distraint or by a proceeding in court (begun before or after the enactment of this Act), but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer before the expiration of such six-year period. The period so agreed upon may be extended by subsequent agreements in writing made before the expiration of the period previously agreed upon."

(2) Section 3770(a) of the Internal Revenue Code (26 U. S. C. A., Sec. 3770(a)) provides in part as follows:

"(2) ASSESSMENTS AND COLLECTIONS AFTER LIMITATION PERIOD.—Any tax (or any interest, penalty, additional amount, or addition to such tax) assessed or paid after the expiration of the period of limitation properly applicable thereto shall be considered an overpayment and shall be credited or refunded to the taxpayer if claim therefor is filed within the period of limitation for filing such claim."

(3) Section 284 of the Revenue Act of 1926 (26 U. S. C. A., Internal Revenue Acts, p. 220) provides in part as follows:

"(b) Except as provided in subdivisions (c), (d), (e) and (g) of this section—

(1) No such credit or refund shall be allowed or made after three years from the time the tax was paid in the case of a tax imposed by this Act, nor after four years from the time the tax was paid in the case of a tax imposed by any prior Act, unless

before the expiration of such period a claim therefor is filed by the taxpayer; and

(2) The amount of the credit or refund shall not exceed the portion of the tax paid during the three or four years, respectively, immediately preceding the filing of the claim, or if no claim was filed, then during the three or four years, respectively, immediately preceding the allowance of the credit or refund."

(4) Section 3772 of the Internal Revenue Code (26 U. S. C. A., Sec. 3772) provides in part as follows:

"(a) LIMITATIONS.—

(1) CLAIM.—No suit or proceeding shall be maintained in any court for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected until a claim for refund or credit has been duly filed with the Commissioner, according to the provisions of law in that regard, and the regulations of the Secretary established in pursuance thereof.

(2) TIME.—No such suit or proceeding shall be begun before the expiration of six months from the date of filing such claim unless the Commissioner renders a decision thereon within that time, nor after the expiration of two years from the date of mailing by registered mail by the Commissioner to the taxpayer of a notice of the disallowance of the part of the claim to which such suit or proceeding relates."

Statement of Facts.

This proceeding was submitted to the District Court on the pleadings, a stipulation of facts and certain exhibits attached thereto [Tr. 11-40], and the oral testimony of the appellant. The appellee introduced no evidence independent of that contained in the stipulation of facts.

The facts here involved, as revealed by the record and as found by the District Court [Tr. 68-72] may be summarized as follows:

(1) On or about October 19, 1929, there was assessed against the appellant an income tax deficiency for the calender year 1925 in the net amount of \$3,472.06, after the allowance of certain credits resulting from overassessments for other years. [Tr. 11, 24, 29, 36 and 41.]

(2) Appellant made payments from time to time until, on August 15, 1933, the balance due on said tax was \$1,255.18, exclusive of interest accruing subsequent to October 19, 1929. [Tr. 3, 8, 12, 34, 36, 41 and 69.]

(3) On August 15, 1932, appellant filed with the Collector of Internal Revenue at Los Angeles, California, an "Offer in Compromise" on Treasury Department Form 656, which contained a waiver, with respect to the statute of limitations, which provided that the appellant, "in the event of the rejection of the offer, expressly consents to the extension of any statute of limitations affecting the collection of the liability sought to be compromised by the period of time (not to exceed two years) elapsed between the

date of the filing of this offer and the date on which final action thereon is taken.” [Tr. 12-13, 18-27, 41-42 and 69.] This document will be sometimes hereinafter referred to as “first offer.”

(4) This first offer and waiver were filed at the request of the Collector of Internal Revenue. [Tr. 42, 69 and 85.] The waiver was accepted in writing by the Commissioner of Internal Revenue on August 25, 1932 [Tr. 13, 21, 42 and 70], and the offer in compromise was rejected in writing by the said Commissioner on October 18, 1932. [Tr. 14, 28, 42 and 70.]

(5) On July 5, 1933, the appellant executed a Treasury Department form entitled “Tax Collection Waiver,” sometimes referred to as an “unlimited waiver,” which provided that the taxes assessed for 1925 “may be collected . . . by distraint or by a proceeding in court begun at any time.” [Tr. 14, 29, 42 and 70.] The said Tax Collection Waiver was executed at the request of the Collector of Internal Revenue [Tr. 42 and 70], and was accepted in writing by the Commissioner of Internal Revenue on March 5, 1934. [Tr. 14, 29, 42 and 70.]

(6) At the time said Tax Collection Waiver was filed, the statute of limitations on collection of the taxes involved herein, as extended by the waiver contained in the first offer, had two years, five months, and seventeen days yet to run. There was, therefore, no apparent reason for requesting it at that time. There was no consideration for the waiver, since no offers in compromise or other proceedings were pending at that time.

(7) On June 11, 1934, the Collector of Internal Revenue abated as uncollectible the balance of \$1,255.18 owed by appellant at that date. [Tr. 34, last line on page.]

(8) On May 21, 1936, appellant filed with the Collector of Internal Revenue at Los Angeles, California, another "Offer in Compromise" on Treasury Department Form 656 which contained a waiver, with respect to the statute of limitations, which provided that the appellant "agrees to the suspension of the running of the statutory period of limitations on assessments and/or collection for the period during which this offer is pending and for one year thereafter." [Tr. 14-15, 30-38, 42-43 and 70-71.] This document will be sometimes hereinafter referred to as "second offer."

(9) This second offer and waiver were filed at the request of the Collector of Internal Revenue. [Tr. 43, 71 and 89.] The waiver was accepted in writing by the Commissioner of Internal Revenue on May 29, 1936 [Tr. 15, 33, 43 and 71], and the offer in compromise was rejected in writing by the said Commissioner on August 9, 1938. [Tr. 16, 38-39, 43 and 71.]

(10) During the period from August 9, 1938, the date on which the second offer of appellant was rejected by the Commissioner of Internal Revenue, to October 9, 1945, the date on which demand for payment was made by appellee, there were no offers in compromise pending or under consideration by the Bureau of Internal Revenue [Tr. 16, 43, 71-72 and

90-93], the appellant had no correspondence or conferences with the Government concerning the taxes involved herein, and the appellee made no attempts to collect said taxes from the appellant. [Tr. 43, 72 and 90-93.]

(11) On October 9, 1945, the appellee made demand upon the appellant for the payment of the balance of said taxes plus interest [Tr. 16, 43 and 72] and on November 14, 1945, the appellant paid to the appellee said balance of \$1,255.18 together with interest in the amount of \$1,904.09, or a total of \$3,159.27. [Tr. 3, 7, 16, 43 and 72.]

(12) On December 11, 1945, the appellant filed with the appellee a claim for the refund of said tax and interest and on June 27, 1946, after more than six months had elapsed, during which time said claim was neither approved nor rejected, the complaint herein was filed. [Tr. 3-6, 10, 43 and 72.]

(13) In the absence of a waiver of the statute of limitations, the collection of the taxes involved herein would have been barred by section 278(d) of the Revenue Act of 1926, *supra*, on October 19, 1935, six years from the date of assessment of said taxes.

(14) The first offer, by its terms extended the statutory period of limitations on collection two months and three days, the time elapsed from the date of filing, August 15, 1932, to the date of rejection, October 18, 1932.

(15) The second offer, by its terms, suspended the running of the statutory period of limitations on col-

lection for three years, two months, and nineteen days, the time elapsed from the date of filing, May 21, 1936, to the date of rejection, August 9, 1938, plus one year.

(16) The appellant's case in the court below was based upon the allegation that the collection of the tax was, on and before November 14, 1945, barred by the statute of limitations on collection and that the payment thereof constituted an overpayment which should be refunded. [Tr. 3.]

(17) The appellee's defense in the court below was based upon the allegation that the appellant had waived the statute of limitations and that the collection of the tax was, therefore, not barred on November 14, 1945. [Tr. 10.]

(18) Unless the Tax Collection Waiver [Tr. 29] was in effect on November 14, 1945, the collection of said tax and interest was clearly barred by the statute of limitations, for the reason that the six-year period provided for by section 278(d) of the Revenue Act of 1926, *supra*, as extended by the first offer, had expired on December 22, 1935. The decision in this case is, therefore, dependent entirely upon a determination as to the validity and/or effect, as of November 14, 1945, of said Tax Collection Waiver.

Specification of Errors.

(1) The District Court erred in concluding that the Tax Collection Waiver executed by appellant on July 5, 1933, was valid. Said waiver did not conform to the provisions of law authorizing waivers in that it purported to waive the statute for all time, whereas section 278(d) of the Revenue Act of 1926 as amended, *supra*, requires that waivers be for a definite period.

(2) Assuming, but not conceding, that the Tax Collection Waiver of July 5, 1933, was not void *ab initio*, the District Court erred in concluding that said waiver was not revoked, superseded, or terminated by the execution and acceptance of the waiver contained in the Offer in Compromise filed on May 21, 1936.

(3) Assuming, but not conceding, that the Tax Collection Waiver of July 5, 1933, was not void *ab initio* and, further, that it was not revoked, superseded, or terminated by the waiver of May 21, 1936, the District Court erred in finding that no unreasonable time elapsed prior to the date when the Government collected the taxes herein involved from the appellant, and in concluding that said Tax Collection Waiver was not rendered inoperative by the lapse of time. The period of more than sixteen years from the date of assessment, October 19, 1929, to the date of collection, November 14, 1945, was manifestly unreasonable and the District Court's finding of fact on this point is wholly unsupported by the evidence.

(4) The District Court erred in concluding that the collection of the taxes involved was not barred by the statute of limitations. The six-year statutory period plus

any and all valid extensions thereof expired many years prior to the date of collection.

(5) The District Court erred in concluding that the appellant has not overpaid the taxes and interest involved herein and is entitled to no relief by his complaint. The payment of taxes after the expiration of the statutory period of limitations constitutes an overpayment as defined by section 3770(a)(2) of the Internal Revenue Code, *supra*.

(6) For all the reasons above set forth, the District Court erred in entering judgment against the appellant and in favor of the appellee.

Summary of Argument.

The taxes involved herein were assessed on October 19, 1929. They were collected on November 14, 1945. The applicable statutory period of limitations expired on October 19, 1935. Unless the statute of limitations was extended by waiver to November 14, 1945, the payment constitutes an overpayment which must be refunded.

Appellant executed and the Commissioner accepted three purported waivers. The first and last contained definite time limitations but the second—the Tax Collection Waiver of July 5, 1933—purported to waive the statute of limitations for all time.

Giving the limited waivers their maximum possible effect, the statutory period of limitations as extended would have expired more than six years prior to the date the taxes were collected; hence our argument will be confined to the question of the validity and effect of the Tax Collection Waiver of July 5, 1933. The discussion will

cover not only the date when given, July 5, 1933, but also the date of collection more than twelve years later, November 14, 1945. This argument will be presented in three alternatives, a favorable decision on any one of which will compel a reversal of the judgment of the District Court. They are as follows:

1. The Tax Collection Waiver of July 5, 1933, was void *ab initio*, hence of no effect at any time.

2. The Tax Collection Waiver of July 5, 1933, if not void *ab initio*, was revoked, superseded, or terminated by the filing and acceptance of the limited waiver contained in the Offer in Compromise filed on May 21, 1936.

3. The Tax Collection Waiver of July 5, 1933, if neither void *ab initio* nor superseded and terminated by the subsequent, limited waiver, was effective only for a reasonable length of time and the time which elapsed from the filing thereof until the collection of the taxes—more than twelve years—was manifestly unreasonable.

Outline of Argument.

A. LEGISLATIVE HISTORY AND GENERAL PRINCIPLES.

B. THE TAX COLLECTION WAIVER OF JULY 5, 1933, WAS VOID *AB INITIO*.

C. THE TAX COLLECTION WAIVER OF JULY 5, 1933, WAS REVOKED, SUPERSEDED, OR TERMINATED BY THE SUBSEQUENT LIMITED WAIVER.

D. THE TAX COLLECTION WAIVER OF JULY 5, 1933, WAS EFFECTIVE ONLY FOR A REASONABLE TIME, AND THAT PERIOD EXPIRED LONG PRIOR TO NOVEMBER 14, 1945.

ARGUMENT.

A. Legislative History and General Principles.

Prior to the Revenue Act of 1918, there was no limitation on the time within which taxes might be collected. Section 250(d) of that Act provided a limit of five years from the due date of the return upon both assessment and collection of the tax. Section 250(d) of the 1921 Act contained a similar provision but measured the time from the filing date instead of the due date of the return.

The 1924 Act contained separate limitation provisions for assessment and for collection, the latter being covered by Section 278(d) which provided for collection “by distraint or by a proceeding in court, begun within six years after the assessment of the tax.”

Section 278(d) of the 1926 Act provided for collection by distraint or by a proceeding in court, “but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer.” This section of the 1926 Act is, by its terms, applicable to taxes for 1925.

The 1928 Act changed the section number to 276(c), added the sentence providing for the extension of the agreed period, and there has been no change in the section since that time. See Historical Note to 26 U. S. C. A., Sec. 276 and volume “Title 26, Internal Revenue Acts.”

The House version of the Revenue Act of 1924 contained no limitation on collection. The Ways and Means

Committee Report, found in Cumulative Bulletin, 1939-1 (Part 2), page 241, explains their attitude on this subject as follows, at page 260:

“ . . . The purpose of a limitation upon assessments is to assure the taxpayer that, after the period has run and no assessment has been made, no taxes may be collected from him. If, however, the assessment is made within the prescribed period, the assessment is comparable to a judgment at law and should remain alive until the tax is paid.”

However, the Senate version, to which the House acquiesced, inserted the six-year limitation, with the following explanation by the Finance Committee in its report at page 288 of the above-mentioned Bulletin:

“ . . . This subdivision in the House bill authorized the collection at any time. . . . In order to protect the taxpayer further, a limitation of six years after the assessment of the tax has been placed upon proceedings in court and distraint for its collection. At the end of such period, the taxpayer is assured that his tax liability is finally determined.”

The intention of Congress to suppress stale tax claims is obvious.

The purpose of a statute of limitations is to suppress and eliminate stale claims and the question whether the claim had any merit in the first instance is immaterial.

A written instrument is to be construed most strongly against the party preparing it and this rule is peculiarly applicable where a printed form is used.

17 C. J. S. 751.

It is a well settled principle of income tax law that doubts as to a waiver's effectiveness must be resolved against the government.

D. J. Gay v. Commissioner, 31 B. T. A. 580, 581 (1934);

Union Shipbuilding Co. v. Commissioner, 43 B. T. A. 1143, 1147 (1941).

The court below dismisses the *Gay* and *Union Shipbuilding* cases with the comment that they differ on their facts and are of no assistance in determining the issues herein. [Tr. 46.] It is true that the facts are not parallel, but that does not affect the force of the general rule of law expounded therein that doubts as to a waiver's effectiveness must be resolved against the government.

The court then proceeds to a brief discussion of cases which hold that statutes imposing limitations upon action by the United States are to be construed in favor of the government.

It is immediately obvious that the court missed the point. We are not here concerned with the construction of a statute but with the construction and interpretation of a written instrument purportedly authorized by the statute. The *statute* is to be construed in favor of the government but the *document* is to be construed in favor of the taxpayer.

B. The Tax Collection Waiver of July 5, 1933, Was Void *Ab Initio*.

The applicable statute of limitations, section 278(d) of the Revenue Act of 1926, *supra*, provides for collection within six years after assessment or "prior to the expiration of any *period* for collection agreed upon in writing by the Commissioner and the taxpayer." (*Italics supplied.*)

"Period" is defined by Webster's New International Dictionary, Unabridged Second Edition (1947) as "a portion or division of time. Specif.: A portion of time as limited and determined by some recurring phenomenon, as by the completion of a revolution of a heavenly body; a division of time, as a series of years, months, or days in which something is completed, and ready to recommence and go on in the same order." It is defined by Bouvier's Law Dictionary as "a stated and recurring interval of time" and by Funk & Wagnalls Practical Standard Dictionary as "a definite portion of time marked and defined by some recurring event or phenomenon."

It follows, therefore, that for a waiver to be valid under the applicable law it must be definite in duration. The Tax Collection Waiver of July 5, 1933, was not; hence it was void *ab initio* because not authorized by the statute.

This precise question, under the law here applicable, has apparently not been heretofore decided. It is respectfully submitted that this court should do so and should determine the issue in appellant's favor for the reasons set forth above.

The court below bases its adverse decision on this point primarily on the absence of cases in support of appellant's contention. It is submitted that the absence of precedent

should not deter this court in deciding the issue as it clearly should be. The court does cite *Cunningham Sheep & Land Co.*, 7 B. T. A. 652 (1927), but that case arose under the 1921 Act which provides that the taxpayer and the Commissioner may consent in writing to “a later determination” and says nothing about collection within a “period” agreed upon. The applicable law was, therefore, quite different from that involved here.

The lower court also appears to accept appellee’s statement on brief that at the time the Tax Collection Waiver was executed there was no statute providing in what manner or for what period the statute of limitations on collection may be waived. This statement is in error. All acts, since waiver provisions first appeared in 1921, have stated that the waivers shall be in writing and, beginning with the 1924 Act as amended the period provided for is that agreed upon—but it must be for some “period” and not for an indefinite time.

C. The Tax Collection Waiver of July 5, 1933, Was Superseded and Terminated by the Limited Waiver of May 21, 1936.

Assuming, but not conceding, that the Tax Collection Waiver of July 5, 1933, was not void *ab initio*, it was effectively superseded and terminated by the limited waiver contained in the second offer in compromise filed on May 21, 1936. (In this connection it must be borne in mind that while the second *offer* was ultimately rejected by the Commissioner, the *waiver* contained therein was accepted by him in writing.)

The two waivers covered the same subject matter, that is, income taxes assessed for the year 1925. They were inconsistent in their terms; the 1933 waiver purported to

waive the statute for all time, whereas the 1936 waiver was effective only for the period during which the offer in compromise was being considered plus one year. They were between the same parties, to wit, the appellant, and the Commissioner.

The Commissioner accepted the 1936 waiver with knowledge of the existence of the 1933 waiver, as indicated by the fact that a copy of the latter was attached to the former in the Commissioner's files. [Tr. 38.] If he had not intended that the 1936 limited waiver should supersede the 1933 unlimited waiver, he would not have accepted the later waiver. It is not to be presumed that the act of signing was meaningless. Furthermore, the 1936 offer containing the limited waiver was filed by appellant at the request of the Government. The intention of the parties is clear.

A case in point is *Helvering v. Ethel D. Co.*, 70 F. 2d 761 (1934), in which the court discusses the principle at some length. As stated by the court in that case:

“* * * If the Commissioner was satisfied that it [the so-called unlimited waiver] conformed to the requirements of the law and rules in relation to waivers and that it was effective to extend indefinitely the time of making the assessment, it was obvious that the second waiver added nothing to what the government already had. Notwithstanding this, the evidence shows the second waiver was accepted and agreed to by the Commissioner.”

The court then went on to apply the invariable rule that where two writings between parties covering the same subject matter are inconsistent with one another, the later one rescinds, supersedes and is substituted for the earlier

one and becomes the only agreement between the parties on the subject.

To the same effect is *Farmers Union State Exchange*, 30 B. T. A. 1051, at 1066 (1934), where the Board said:

“The two waivers must be construed together.
* * * To say that the first waiver remained in effect after the execution of the second waiver, under the circumstances set out, would be equivalent to brushing aside the meaning of the later waiver. It must have been intended that the second waiver should be substituted for the unlimited waiver.”

The above quoted language can and should be applied to our case without change. The 1933 and 1936 waivers covered the same subject matter between the same parties and were inconsistent in their terms. Therefore, the later, limited waiver must be held to have rescinded, superseded, and been substituted for the earlier, unlimited waiver.

Any other conclusion would render meaningless the joint act of the parties and such a result is not to be presumed. This is particularly true where, as here, the form of agreement used is a printed form provided by the Government and is filed at the Government's request. As heretofore pointed out, the effect thereof shall be construed most strongly against the party which provides the document.

The lower court again misses the point when it dismisses the case of *Atlantic Mills of Rhode Island v. U. S.*, 3 Fed. Supp. 699 (1933), cited on brief below, with the comment that the issue therein is not present in this case. [Tr. 47.] That case was and is cited on the simple proposition that a waiver is not effective until signed by the

Commissioner. True, all waivers involved herein were so signed, and that is just the point.

If the limited waiver of May 21, 1936, had not been signed by the Commissioner, it would have been of no effect and the unlimited Tax Collection Waiver of July 5, 1933, would have continued in effect (assuming for the sake of this argument that it did not fall or expire for one of the other reasons advanced by this brief); but the Commissioner did sign, and in so doing performed an act which is required in order to give effect to the instrument. The only possible effect of the limited waiver was to revoke, terminate and supersede the unlimited waiver. Consequently, the obvious—in fact, the only—conclusion to be drawn from these facts is that the Commissioner, having performed an affirmative act, must have intended it to be effective.

Proceeding from the foregoing, it is a matter of simple calculation to determine that the statute of limitations on the collection of the taxes involved herein expired not later than August 9, 1939, more than six years prior to the date of collection.

The court below quotes at length from *U. S. v. Fischer*, 93 F. 2d 488 (1937) and *Atlantic Mills of Rhode Island v. United States*, *supra*, and concludes therefrom that the unlimited waiver was not terminated “by the giving” of the limited waiver. (Italics supplied.)

The appellant does not contend that *the giving* of the limited waiver terminated the unlimited waiver, but the appellant does contend that the joint act of appellant and the Commissioner in *executing and making effective* the limited waiver did revoke, terminate, and supersede the unlimited waiver.

In the *Atlantic Mills* case, *supra*, it was held that the giving of a waiver, which was not signed by the Commissioner, did not constitute a notice by the taxpayer of termination of a prior unlimited waiver. In our case, the limited waiver was given to and signed by the Commissioner, thus presenting an entirely different situation. A definite period was set by agreement in our case whereas the Commissioner refused to do so in the *Atlantic Mills* case.

The *Fischer* case, *supra*, involved two limited waivers rather than an unlimited one followed by a limited one, as in our case, which is a distinguishing feature. But more important is the difference in the circumstances under which the waivers were given in the two cases. In the *Fischer* case the first waiver was given in connection with an offer in compromise and held the statute open while the government considered the offer. The second waiver was executed subsequently, not in connection with an offer, and, so far as the case reveals, totally unrelated to the offer already on file. The government was still considering the offer when the time set by the second waiver expired. The Circuit Court ruled that, under the circumstances, the second did not supersede the first.

In our case, when the unlimited waiver was given on July 5, 1933, no offer or other proceeding was pending and the government had two years, five months and seventeen days left in which to collect the tax without further waivers. Furthermore, on June 11, 1934, three months after the Commissioner signed the waiver, the government wrote the appellant's account off its books, indicating it was no longer interested in trying to collect. The balance was abated nearly a year and a half before the un-

extended six-year statutory period of limitations would have expired. There was, then, no need for a waiver at that time. On the other hand, the subsequent limited waiver was filed in connection with an offer in compromise and served a definite purpose in protecting the government while it considered the offer. The situation was just the reverse of that in the *Fischer* case, and it is submitted that the decision should be the reverse, also.

Of course, the appellee will argue that waivers are unilateral undertakings, are not contract, and require no consideration; hence the foregoing differences in circumstances are immaterial. That the circumstances are material is indicated by the *Fischer* case where the court points out, at page 489, that "The defendant obtained consideration of his compromise offer by agreeing that the statute of limitations should be extended as therein provided."

The court below would let the government have its cake and eat it too, judging from the following quotation from the opinion [Tr. 56]:

" . . . It is logical to assume that when the Commissioner requested the third waiver, he intended to secure a fixed period within which he might consider the compromise offer and investigate the financial status of the taxpayer, during which period, in the event the taxpayer filed notice of termination of the unlimited waiver, the Commissioner would not be left without a waiver."

We agree that the Commissioner intended to secure a fixed period, but do not agree that he did not thereby relinquish the unlimited waiver. One waiver is sufficient to

protect the government. Why should it be permitted to insist on two?

By its terms, the last waiver gave the government a full year in which to act after the offer was rejected. In this connection it should be borne in mind that collection does not have to be accomplished within the time limit. The statute is satisfied if proceedings are begun, by distraint or suit in court, within that time. Thus the government could have protected itself fully at any time prior to the expiration of the statute as extended by filing suit and obtaining a judgment against the appellant.

D. The Tax Collection Waiver of July 5, 1933, Was Effective Only for a Reasonable Time.

Following the principle of contract cases that where time for performance is not specified a reasonable time will be allowed, the Board of Tax Appeals many years ago adopted the rule that waivers which are not limited as to time give the government a reasonable time within which to act.

Herman Frost v. Commissioner, 23 B. T. A. 411 (1931);

Nathan Loeser v. Commissioner, 27 B. T. A. 601 (1933).

Those cases, and earlier cases cited therein, held periods of time varying from one and a half years to five and a half years to be reasonable. In all of the cases refund claims, protests, or litigation were pending and these pending matters had to be settled before proper tax liability could be determined. It was therefore held in each case that, in view of these circumstances, the time which had elapsed was not more than a reasonable time.

In our case the elapsed time from the date of filing of the second or so-called unlimited waiver, to the date of collection of the tax amounts to twelve years, four months and nine days, during the last seven years, three months and five days of which time there were no proceedings of any sort had or pending between the plaintiff and the government.

If we consider only the period from the expiration of the statute as extended by the first waiver, or December 22, 1935, to the date of payment of the tax, we find that the elapsed time was almost ten years. This is obviously more than a reasonable length of time when it is noted that no proceedings were pending during more than seven years of this period.

The defendant will, of course, cite *Greylock Mills v. Commissioner*, 31 F. 2d 655 (C. C. A. 2, 1929), as authority for the rule that the so-called unlimited waivers continue in effect until reasonable notice of termination has been given by either party.

This statement by the court was pure dictum, the decision of the Board of Tax Appeals having already been upheld upon the basis of its finding of fact that the period of time was reasonable. The rule propounded cannot, therefore, be considered as binding.

No case has ever been decided solely on the basis of this rule. Other circuit courts have expressly refused to accept or reject it, *Greylock Mills v. White*, 63 F. 2d 866 (C. C. A. 1, 1933). In *Helvering v. Ethel D. Co.*, *supra*,

the Circuit Court of Appeals for the District of Columbia, after quoting from the Second Circuit's opinion to the effect that notice was required, stated that it was "disposed to think that the waiver would fall of itself after a reasonable time" without the necessity of notice by either party.

We think the proper rule and the one which the Second Circuit would have adopted if the question had been necessary to the decision of its case and had been carefully considered, is as stated in *Farmers Union State Exchange v. Commissioner, supra*, that "an unlimited waiver does not suspend the running of the statute forever, but only for a reasonable time or until termination by either party upon reasonable notice." In other words, such a waiver is good for a reasonable time *unless terminated sooner* upon notice by either party.

In our case it is submitted that the length of time during which the second waiver must have been effective in order for the defendant to prevail was so extremely long that the waiver must have long since fallen of its own weight and that no notice by the taxpayer was necessary.

A decision that the 1933 waiver fell of its own weight after a reasonable time will recognize the expressed intent of Congress "to protect the taxpayer."

The court below found as a fact that no unreasonable time elapsed. [Tr. 72.] There is no evidence in the record to support such a finding. In fact, the evidence is all to the contrary, as pointed out above.

Conclusion.

In conclusion, appellant respectfully submits that the decision and judgment herein should be reversed for the reason that the collection of the taxes herein involved was, on November 14, 1945, the date of payment by the appellant, barred by the provisions of the applicable statute of limitations.

Respectfully submitted,

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No. 11973

IN THE

United States Court of Appeals
FOR THE NINTH CIRCUIT

E. C. SIMMONS,

Appellant,

vs.

HARRY C. WESTOVER, Collector of Internal Revenue,

Appellee.

**Appeal From the District Court of the United States
for the Southern District of California,**

BRIEF FOR THE APPELLEE.

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No. 11973

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

E. C. SIMMONS,

Appellant,

vs.

HARRY C. WESTOVER, Collector of Internal Revenue,

Appellee.

BRIEF FOR THE APPELLEE.

Opinion Below.

The opinion of the District Court [R. 41-67] is reported at 76 Fed. Supp. 442.

Jurisdiction.

This appeal involves federal income taxes for the year 1925. The taxes in dispute, in the amount of \$1,255.18, plus assessed interest of \$1,904.09, a total of \$3,159.27, were paid on November 14, 1945. [R. 72.] A claim for refund was filed on December 11, 1945. [R. 3-4, 10.] No decision thereon was rendered within six months, and on June 27, 1946, the taxpayer brought this action in the District Court for recovery of the taxes. [R. 6, 72.] Jurisdiction was conferred on the District Court by Section 24, Twentieth, of the Judicial Code. The judgment was entered in favor of the Collector on April 26, 1948. [R. 74-75.] Within sixty days thereafter and on June 21, 1948, a notice of appeal was filed [R. 75], pursuant to the provisions of 28 U. S. C., Section 1291.

Question Presented.

Whether the balance of an assessment of additional income tax for the year 1925, in the amount of \$1,255.18, plus assessed interest of \$1,904.09 (a total of \$3,159.27), paid on November 14, 1945, was paid after the expiration of the period of limitation applicable thereto, and hence was an overpayment within the meaning of Section 3770 (a)(2) of the Internal Revenue Code, as contended by the taxpayer; or was paid within the period of limitation as extended by an unlimited collection waiver, which remained in full force and effect at the time of the payment, as determined by the Commissioner.

Statutes Involved.

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 278 (as amended by Sec. 506(a), Revenue Act of 1928, c. 852, 45 Stat. 791). * * *

(d) Where the assessment of any income, excess-profits or war-profits taxes imposed by this title or by prior Act of Congress has been made (whether before, or after the enactment of this Act) within the period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding in Court (begun before or after the enactment of this Act), but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer before the expiration of such six-year period. The period so agreed upon may be extended by subsequent agreements in writing made before the expiration of the period previously agreed upon.

* * * *

Internal Revenue Code:

CHAPTER 1—INCOME TAX

SEC. 1. APPLICATION OF CHAPTER.

The provisions of this chapter shall apply only to taxable years beginning after December 31, 1938. Income, war-profits, and excess-profits taxes for taxable years beginning prior to January 1, 1939, shall not be affected by the provisions of this chapter, but shall remain subject to the applicable provisions of the Revenue Act of 1938 and prior revenue acts, except as such provisions are modified by legislation enacted subsequent to the Revenue Act of 1938. (26 U. S. C. 1946 ed., Sec. 1.)

SEC. 3770. AUTHORITY TO MAKE ABATEMENTS,
CREDITS, AND REFUNDS.

(a) *To Taxpayers.*—

(1) *Assessments and collections generally.*—

* * *

(2) *Assessments and collections after limitation period.*—Any tax (or any interest, penalty, additional amount, or addition to such tax) assessed or paid after the expiration of the period of limitation properly applicable thereto shall be considered an overpayment and shall be credited or refunded to the taxpayer if claim therefor is filed within the period of limitation for filing such claim. (26 U. S. C. 1946 ed. Sec. 3770.)

Statement.

The essential facts, taken from the findings of the court below, are as follows:

On or about October 19, 1929, income taxes for the year 1925 were assessed against the taxpayer. Over-assessments for other years were credited against the amount assessed, leaving a balance of \$3,723.06. After notice and demand, a warrant of distraint was issued with respect to the liability, and on December 19, 1929, notice of lien was filed with the Recorder of Los Angeles County, California. [R. 69.]

The taxpayer made payments from time to time in amounts varying from \$75 to \$250 on the outstanding balance, until August 15, 1933, at which time the balance due was the sum of \$1,255.18, with interest thereon. [R. 69.] On August 1, 1932, the taxpayer executed an "Offer in Compromise" on Treasury Department Form 656, a printed form including a waiver with respect to the statute of limitations, which waiver provided that the taxpayer waived the benefit of any statute of limitations affecting the collection of the liability sought to be compromised and in the event of the rejection of the offer, expressly consented to the extension of any statute of limitations affecting such liability, by the period of time, not exceeding two years elapsed between the date of the filing of the offer and the date on which final action thereon should be taken. The offer and waiver were executed at the request of the Collector of Internal Revenue at Los Angeles, and were filed with such collector

on August 15, 1932. [R. 69.] The taxpayer attached to the foregoing offer his letter dated July 20, 1932, addressed to the Commissioner of Internal Revenue, wherein the taxpayer enclosed a financial statement which showed liabilities in the amount of \$32,482.73, which was in excess of his assets. [R. 70.] Such excess amounted to \$32,283.35½. [R. 25.] The taxpayer stated in the letter that if his financial status became known to his employer he would lose his position. [R. 70.] On August 25, 1932, the Commissioner of Internal Revenue accepted in writing the taxpayer's "Waiver of Statute of Limitations," and on October 18, 1932, rejected the "Offer in Compromise." [R. 70.]

On July 5, 1933, at the request of the Collector of Internal Revenue, the taxpayer executed a "Tax Collection Waiver," wherein it was agreed between the Commissioner of Internal Revenue and the taxpayer that the amount of \$3,472.06, representing as assessment of income taxes for the year 1925, might be collected, with interest, from the taxpayer by distraint or by a proceeding in court begun at any time. At that time, no offer in compromise was pending and the waiver was not submitted in connection with any offer in compromise. The waiver was accepted by the Commissioner on March 5, 1934. [R. 70.]

On May 6, 1936, the taxpayer executed an "Offer in Compromise" on Treasury Department Form 656, a printed form including a waiver with respect to the statute of limitations, which waiver provided that the taxpayer waived the benefit of any statute of limitations

affecting the collection of the liability sought to be compromised, and agreed to the suspension of the statutory period of limitations on assessment or collection for any period during which the offer should be pending and for one year thereafter. The taxpayer tendered with the offer the sum of one hundred dollars in settlement of the balance due, and stated in the offer that he had been without income for several years and had subsisted largely on borrowed money. He included with the offer a financial statement which showed his liabilities in excess of his assets by the amount of \$28,698.35. The offer and waiver were executed at the request of the Collector of Internal Revenue at Los Angeles and were filed with such Collector on May 21, 1936. The Collector transmitted the offer and waiver to the Commissioner of Internal Revenue, forwarding therewith a copy of the Tax Collection Waiver filed July 5, 1933. The waiver executed May 6, 1936 was accepted by the Commissioner of Internal Revenue in writing on May 29, 1936, and the offer submitted at the time of such waiver was rejected by the Commissioner on August 9, 1938. [R. 70-71.]

After August 9, 1938, no offer in compromise from the taxpayer was pending or under consideration by the Bureau of Internal Revenue, and from such date of August 9, 1938, until October 9, 1945, the taxpayer had no correspondence or conferences with the Government concerning the taxes involved, and, to the taxpayer's knowledge, no attempts were made during that period to collect such taxes. [R. 71-72.] On October 9, 1945,

the Collector of Internal Revenue made demand on the taxpayer for the payment of the taxes, and on November 14, 1945, the taxpayer paid the balance of \$1,255.18, plus interest of \$1,904.09, and fifty cents for release of the lien hereinabove mentioned. Thereafter, the taxpayer filed a claim for refund of the amount of the taxes and interest so paid. After the lapse of six months from the filing of the claim without action by the Commissioner, the taxpayer brought the instant action. [R. 72.]

No notice with respect to revoking the Tax Collection waiver of July 5, 1933, was given by the taxpayer. [R. 72.]

Under all the circumstances, no unreasonable time elapsed prior to the date when the Government collected from the taxpayer the taxes herein involved. [R. 72.]

The District Court concluded that the Tax Collection Waiver of July 5, 1933, was valid; that it was not revoked or terminated by the execution and acceptance of the waiver of May 6, 1936; that it was not revoked or terminated by the lapse of time; that it was operative at the time the taxes in question were collected; that the payment of the taxes and interest herein did not constitute an overpayment, and that the defendant Collector was entitled to judgment with costs. [R. 73.]

Summary of Argument.

The taxes in question were collected within the period of limitation as extended by an unlimited waiver which remained in full force and effect at the time of payment.

The collection of the tax was authorized by Section 278 (d) of the Revenue Act of 1926, as amended. The collection was made while an unlimited waiver given by the taxpayer was in full force and effect.

The unlimited waiver was not terminated by an offer in compromise made in 1936, with an accompanying waiver.

The unlimited waiver could not be revoked or terminated by mere lapse of time, but only upon reasonable notice given by the taxpayer, and no such notice was given.

Even if the unlimited waiver was effective only for a reasonable time, the collection of the tax in question, under the circumstances herein, was made within a reasonable time.

There is a presumption that taxes paid are rightly collected upon assessments correctly made by the Commissioner, and in a suit to recover them the burden rests upon the taxpayer to prove all the facts necessary to establish the illegality of the collection. The taxpayer has not sustained that burden in the instant action.

A suit for refund of taxes is governed by equitable principles and the taxpayer must recover by virtue of a right measured by equitable standards.

If the taxpayer was unable to pay the taxes prior to 1945 he has no real ground for complaint as to the delay. If he was able to pay, the delay in payment was as much due to the taxpayer's wrong as to the failure of the tax officials. He should not be permitted to take advantage of his own wrong.

ARGUMENT.

The Taxes in Question Were Collected Within the Period of Limitation as Extended by an Unlimited Waiver Which Remained in Full Force and Effect at the Time of the Payment.

No issue is raised in the taxpayer's complaint [R. 2-4] as to the due and timely assessment of the taxes, and no such issue has been suggested at any time during the presentation of the case. Both parties have assumed that the assessment was timely made, and both have relied upon the statutory provisions pertaining to the collection of taxes after assessment has been made "within the period of limitation properly applicable thereto." Sec. 278(d) of the Revenue Act of 1926, as amended, *supra*. Hence, the discussion herein assumes the timely assessment of the tax.

We agree with the position of the taxpayer (Br. 9) that the tax in question was paid after the period of limitation had expired, unless the Tax Collection Waiver of July 5, 1933, which will be hereinafter referred to as the unlimited waiver, was effective to keep the limitation period open.

A. The Collection of the Tax in Question Was Authorized by Section 278(d) of the Revenue Act of 1926, as Amended.

The period provided for collection in Section 278 (d) of the Revenue Act of 1926, as amended, *supra*, is six years, after assessment, but this period may be extended by agreement. The tax was assessed on or about October 19, 1929, pursuant to an agreement between the taxpayer and the Commissioner. [R. 11-69.] Without extension,

the collection period would therefore have expired on or about October, 1935. While there was some extension of this time by the waiver contained in the 1932 offer in compromise [R. 69, 70], and there was afterward, in 1936, another similar extension, it is the unlimited waiver upon which the Government relies to support the collection. Under this waiver, the collection was made prior to the expiration of the period agreed upon in writing within the meaning of Section 278 (d), as amended, *supra*.

The taxpayer argues (Br. 16) that the unlimited waiver was void *ab initio* because it was not definite in duration. Such a contention was rejected by the Board of Tax Appeals in *Cunningham Sheep & Land Co. v. Commissioner*, 7 B. T. A. 652, 655. The taxpayer asserts (Br. 17) that the *Cunningham* case arose under the Revenue Act of 1921, Section 250(d) of which provides that the taxpayer and the Commissioner may consent to "a later determination" but says nothing about collection within a "period" agreed upon. However, it is to be noted that in that case the Board considered the applicability of Section 278 (c) of the Revenue Act of 1924, which provided that where the Commissioner and the taxpayer had consented in writing to the assessment of the tax after the time prescribed in Section 277, the tax might be assessed at any time "prior to the expiration of the period agreed upon," and said that the consent there involved, which was to a determination, assessment and collection of taxes irrespective of any period of limitations, was sufficient to meet the requirements of such Section 278 (c).

The validity of unlimited waivers was also sustained in *Stange v. United States*, 282 U. S. 270, and *Big Four Oil & Gas Co. v. Heiner*, 57 F. 2d 29 (C. C. A. 3rd).

B. The Unlimited Waiver Was Not Superseded or Terminated by the Limited Waiver Which Accompanied the 1936 Offer in Compromise.

In support of his position that the unlimited waiver was superseded or terminated by the 1936 waiver, the taxpayer cites (Br. 18) *Helvering v. Ethel D. Co.*, 70 F. 2d 761 (App. D. C.). The decision of the court that the unlimited waiver in that case was superseded by the later definite waiver was based on the finding that such was the intention of both the Government and the taxpayer. The circumstances pointing to such intention there are not present in the instant case. The waiver there was requested by the Government apart from and not as incidental to an offer in compromise as was the 1936 waiver in the instant case. The unlimited waiver there was on a form then being abandoned and a new form was being used. The 1936 waiver in the instant case was on a printed form of offer in compromise, and the waiver was incidental to the offer. The new waiver in the *Ethel* case fixed a definite date (December 31, 1925) for the termination of the limitation period, while in the instant case, the 1936 waiver merely suspended the running of the statute for a certain period. The new waiver in the *Ethel* case was requested by the Government and was submitted immediately after the unlimited waiver, and it was definitely understood by both parties that it was asked for and submitted because the unlimited waiver was unsatisfactory. The circumstances are so different that the *Ethel* case can furnish no support for a similar decision in the instant case. In the *Ethel* case, the court said that the new waiver was a sufficient notice to effect a termination of the unlimited waiver as of that date.

In the instant case, the District Court found as a fact that no notice with respect to the termination of the unlimited waiver had been given by the taxpayer. [R. 72.] This implies a finding that the 1936 waiver was not intended as such a termination, and it was clearly not an erroneous finding.

The Taxpayer argues (Br. 22-23) that the 1936 waiver could serve no purpose if the unlimited waiver was operative, but clearly it could serve the purpose of giving the Commissioner a time certain within which to consider the offer submitted, even if the taxpayer at any time gave notice of the termination of the unlimited waiver and regardless of what might be held later as to a reasonable time for the running of the unlimited waiver.

The taxpayer also cites (Br. 19) *Farmers Union State Exchange v. Commissioner*, 30 B. T. A. 1051. The Board there treated the question whether the unlimited waiver was terminated by a later limited waiver as depending on intent, and said (p. 1068) that it must have been intended that the limited waiver should be substituted for the unlimited waiver. The Board noted that the second waiver was executed before the unlimited waiver became effective. In the instant case, the unlimited waiver had been effective from 1933 to 1936, when the limited waiver was executed. In the *Farmers* case like the *Ethel* case, *supra*, the later waiver involved fixed the time of the extension provided for by referring in terms to the expiration of the limitation period. In the *Farmers* case, the later waiver was to be effective for a period of one year after the expiration of the statutory period as previously extended. In the instant case, the limited waiver of 1936 does not in terms provide any date whatever with respect to the expiration of the limitation period. It merely provides for the

suspension of the running of the statutory period for the period during which the offer should be pending and for one year thereafter. [R. 71.]

A provision relative to the suspension of the statute is not equivalent to a provision providing for the expiration of the statute or fixing a date with respect to such expiration. The suspension provision in the limited waiver in the instant case hinged upon the pendency of the offer, and was wholly apart from and independent of any expiration date. *United States v. Markowitz*, 34 F. Supp. 827 (N. D. Cal.); *Olds & Whipple v. United States*, 22 F. Supp. 809 (C. Cls.); *United States v. Bank of Commerce & Trust Co.*, 32 F. Supp. 942 (W. D. Tenn.) Under the reasoning of the cases just cited, the end of a suspension period does not mean that the statute then expires, but rather, when the suspension period ends, it is necessary to refer to the *status quo* before the suspension period began and then add after the end of the suspension period whatever time and allow whatever rights the Government had prior to the beginning of the period. Prior to the suspension period under the limited waiver here involved (commencing on May 21, 1936, when the 1936 waiver was filed) the Government had unlimited waiver rights under the 1933 unlimited waiver. Those rights automatically continued when the suspension period here ended in 1939, and the statute resumed its running.

Another case in point is *United States v. Fischer*, 93 F. 2d 488, 489 (C. C. A. 2d). This was an action by the United States to collect taxes due from the taxpayer. The action was barred unless a waiver given by the taxpayer in January, 1932, in connection with an offer in compromise was controlling. That waiver extended the statute by the period of time (not exceeding two years)

which had elapsed between the date of filing of the offer and the date of final action thereon. The offer was pending approximately two years. The action was within that extension period. The lower court, however, had held that first waiver not controlling on the ground that it had been superseded by two later waivers given in February, 1932, which extended the time for collection either by distraint or by a proceeding in court begun at any time before December 31, 1933. The second Circuit Court of Appeals reversed the judgment, holding that the extension effected by the first waiver was not reduced by the later waivers, since the Government relinquished no rights by accepting them. It is to be noted, in view of the taxpayer's comment (Br. 20-21), that the later waivers were not merely given but were accepted also.

By the 1936 waiver, in the instant case, the taxpayer and the Government recognized the efficacy of the unlimited waiver. In the absence of any waiver, the six year statute would have expired six years after October 19, 1929, or on October 19, 1935. The 1932 waiver had extended the statute for two months and three days, which period would carry from October 19, 1935, to December 22, 1935. This latter date would have been the expiration date if there had been no waiver subsequent to the 1932 waiver. Hence, the statute would have expired in 1935 but for the 1933 unlimited waiver. When he entered into the 1936 waiver, the taxpayer recognized the statute as "running" and not as having run or expired. The 1936 waiver provided that such "running" was to be suspended for a definite period of time. If the statute was not running when the 1936 waiver was filed, then the taxpayer who executed the waiver and the Commissioner who accepted it were acting under a mutual mis-

take, and accordingly, the 1936 waiver can be avoided on that ground, whether the mistake be deemed one of fact (*Davies v. Lahann*, 145 F. 2d 656, 660 (C. C. A. 10th); *Fidelity & Deposit Co. of Maryland v. McQuade*, 123 F. 2d 337, 339 (App. D. C.)), or one of law (*S. S. Pierce Co. v. United States*, 17 F. Supp. 667, 669 (Mass.), and cases there cited).

Regardless of whether the statute was or was not "running" when the 1936 waiver was filed, it follows from the foregoing that in either event the taxpayer's reliance upon such waiver to supersede the unlimited waiver is in vain for the reason that that waiver either operated as a mere suspension of the statute, which after the suspension resumed running, or else it accomplished nothing whatsoever.

C. The Unlimited Waiver Could Not Be Revoked or Terminated by Mere Lapse of Time, but Only Upon Reasonable Notice Given by the Taxpayer, and No Such Notice Was Given.

A waiver which is in terms unlimited as to time expires only upon reasonable notice to that effect given by the taxpayer. *Greylock Mills v. Commissioner*, 31 F. 2d 655, 658 (C. C. A. 2d); *Big Four Oil & Gas Co. v. Heiner*, 57 F. 2d 29, 30-31 (C. C. A. 3d); *Warner Sugar Refining Co. v. Commissioner*, 4 B. T. A. 5, 11-12; *Bateman v. Commissioner*, 34 B. T. A. 351, 358. No notice was given by the taxpayer with respect to the termination of the unlimited waiver here involved. [R. 72.] That the 1936 limited waiver did not constitute such notice was shown under point B above. The unlimited waiver therefore remained in effect when the tax in question was paid.

D. Even if the Unlimited Waiver Was Effective Only for a Reasonable Time, the Collection of the Tax in Question, Under the Circumstances Herein, Was Made Within a Reasonable Time.

Even if the unlimited waiver was effective only for a reasonable time, it is clear that the collection of the tax here involved was made within such time. In determining what is a reasonable time for collection, it seems obvious, that account must be taken of the taxpayer's financial condition, among other circumstances. In his letter of July 20, 1932 [Ex. A-3, R. 24-25], which was submitted with his first offer in compromise, he stated that he was unable to pay in a lump sum the balance then due, and that after making some installment payments, the last of which was made on July 8, 1932, his financial condition had grown worse, that his salary had been cut, that he owed a number of other debts, that he had to keep up a certain front in order to maintain his position, and that if it were known he was bankrupt, his "term would be short indeed." He submitted a statement of assets and liabilities, showing liabilities exceeding assets by the amount of \$32,283.35½. [Ex. A-4, R. 26-27.)

The taxpayer submitted a new offer in compromise which was dated May 6, 1936, and filed May 29, 1936. [Ex. D-1, R. 30-33.] This was an offer of \$100, in addition to \$2,216.88 referred to as already paid. He stated that he had been for several years without regular income and had been subsisting on borrowed money. His

financial statement at that time [Ex. D-4, R. 37] showed liabilities in excess of assets by the amount of \$28,698.35.

The record thus shows that by his own representation, he was in an insolvent condition in 1932 and that it continued for at least four years. Such a condition once shown to exist is presumed to continue in the absence of evidence to rebut the presumption. The presumption applies to a person's financial condition and specifically to insolvency. *Mount Vernon Hotel Co. v. Block*, 157 F. 2d 637, 639 (C. C. A. 9th); *Dunbar v. Commissioner*, 119 F. 2d 367, 370 (C. C. A. 7th); *Cleage v. Laidley*, 149 Fed. 346, 354 (C. C. A. 8th). The duration of the presumption depends of course on the circumstances. It had continued by the taxpayer's own representations for four years. In this case, a duty rested on the taxpayer to make payment as soon as he was able. Section 145 (a) of the Internal Revenue Code (26 U. S. C. 1946 ed., Sec. 145(a)), provides a heavy penalty for wilful failure to pay a tax. The taxes were admittedly justly due and owing, and so far as lapse of time is concerned, it was a penal offense for the taxpayer not to pay the taxes if he was able to do so. The taxpayer has no real ground for complaint as to delay in the absence of a showing that efforts to collect would not have been futile. He has made no such showing.

Taking all the circumstances into account, there was no unreasonable delay in the collection of the taxes in question. The District Court so found. [R. 72.]

The presumption is that taxes paid are rightly collected upon assessments correctly made by the Commissioner, and in a suit to recover them the burden rests upon the taxpayer to prove all the facts necessary to establish the illegality of the collection. *Niles Bement Pond Co. v. United States*, 281 U. S. 357, 361; *United States v. Anderson*, 269 U. S. 422; see *United States v. Rindskopf*, 105 U. S. 418. This rule as to the burden resting on the taxpayer applies where the taxpayer is asserting the expiration of the statutory period. *Tooley v. Commissioner*, 121 F. 2d 353 (C. C. A. 9th). A suit for refund of taxes is governed by equitable principles and the taxpayer must recover by virtue of a right measured by equitable standards. *United States v. Jefferson Electric Co.*, 291 U. S. 386, 402; *Stone v. White*, 301 U. S. 532, 534-535; *Ryan v. Alexander*, 118 F. 2d 744 (C. C. A. 10th).

If collection of these taxes was possible prior to October 9, 1945, the date of the Collector's final demand, the delay in payment beyond that time was at least as much due to the taxpayer's wrong as to the failure of the tax officials. It is a fundamental principle that no one can take advantage of his own wrong. This principle should particularly apply in a proceeding of an equitable nature such as the instant action.

Conclusion.

The judgment of the District Court should be affirmed.

Respectfully submitted,

THERON LAMAR CAUDLE,
Assistant Attorney General.

ELLIS N. SLACK,
ROBERT N. ANDERSON,
JOHN W. FISHER,
*Special Assistants to the
Attorney General.*

JAMES M. CARTER,
United States Attorney.

E. H. MITCHELL,
Assistant United States Attorney.

GEORGE M. BRYANT,
Assistant United States Attorney.

EUGENE HARPOLE,
Special Attorney, Bureau of Internal Revenue.

November, 1948.



No. 11973

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

E. C. SIMMONS,

Appellant,

vs.

HENRY C. WESTOVER, Collector of Internal Revenue,

Appellee.

REPLY BRIEF FOR APPELLANT.

LATHAM & WATKINS,

1112 Title Guarantee Building, Los Angeles 13,

Attorneys for Appellant.

FILED

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PAUL P. O'BRIEN,

TOPICAL INDEX

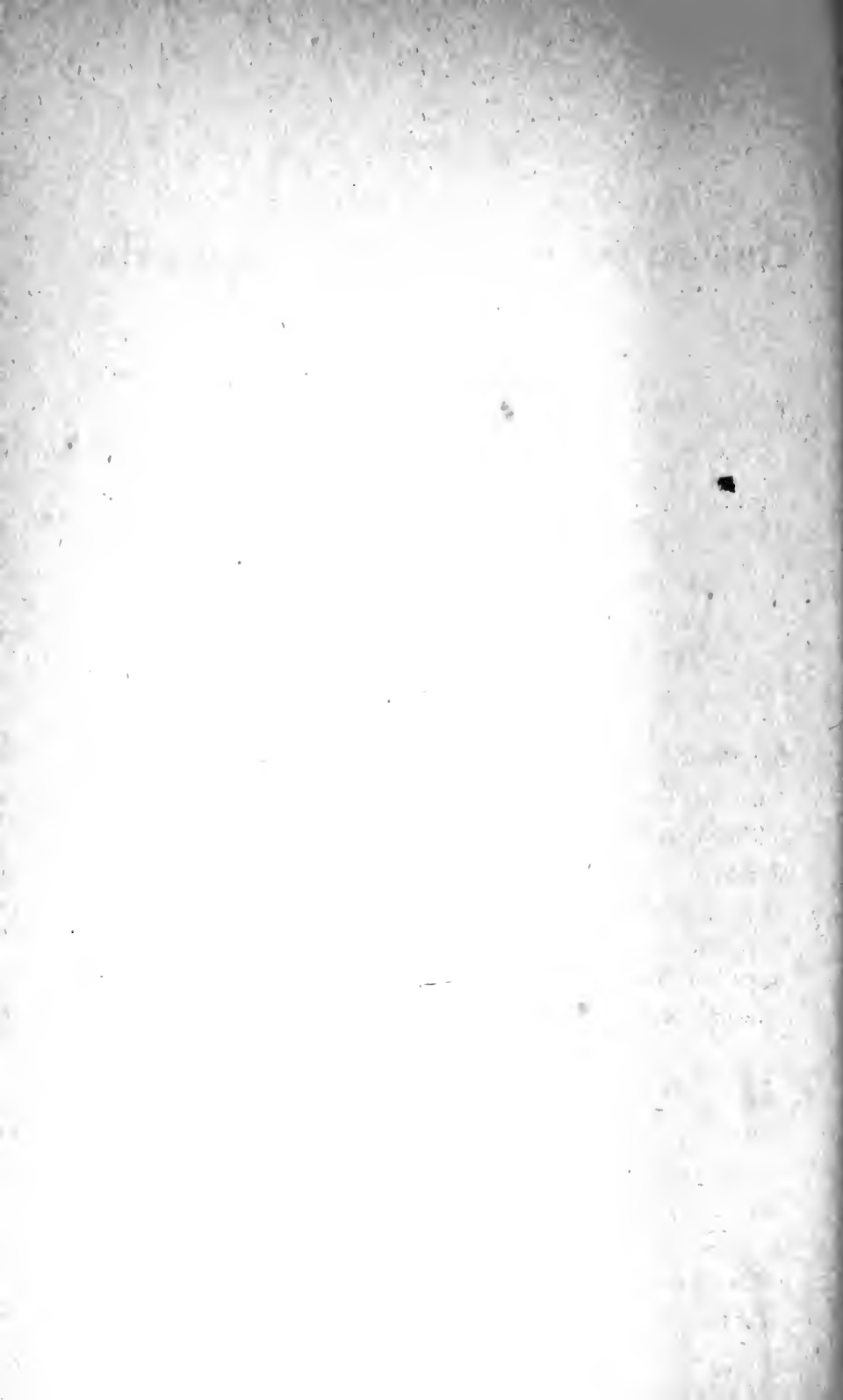
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No. 11973

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

E. C. SIMMONS,

Appellant,

vs.

HENRY C. WESTOVER, Collector of Internal Revenue,

Appellee.

REPLY BRIEF FOR APPELLANT.

Appellee Confuses the Legal Principles Applicable to This Proceeding.

The Appellee in his brief has cited numerous cases as authority for his statements of legal principles applicable to this proceeding. Because some of the statements are misleading and are not supported by the cases cited, the Appellant deems it necessary to comment on some of these citations in this reply brief.

At the bottom of page 10 of his brief, the Appellee cites *Stange v. U. S.*, 282 U. S. 270, and *Big Four Oil and Gas Co. v. Heiner*, 57 F. 2d 29, as upholding the validity of unlimited waivers. In neither of these cases was a decision on this issue necessary and both cases arose under revenue acts which did not require that the extension of the statutory period of limitations be for a "period." In the *Stange* case, the issues decided were whether the exe-

cution of a waiver after the expiration of the statute was effective and whether a consent to the determination of the liability included a consent to its collection. In the *Big Four Oil and Gas* case, the Court found that the Revenue Act of 1926 intervened and provided retroactively for collection of the tax within six years, and that the tax involved had been collected within six years. Thus, neither of these cases is direct authority for the statement made by the Appellee.

At page 11 of his brief, in commenting upon the case of *Helvering v. Ethel D. Co.*, 70 F. 2d 761, the Appellee makes certain statements which are not entirely accurate. He states that it was "definitely understood by both parties" in that case that the limited waiver was submitted because the unlimited waiver was unsatisfactory. A reading of the case discloses that the conclusion that the parties so understood and intended that the second waiver superseded the first was based upon inferences and not upon a finding of a "definite understanding." As stated in Appellant's opening brief, at page 18, the Court found that the parties must have intended the second waiver to supersede the first, because the second would have had no effect otherwise.

The Appellee further states that in the *Ethel D.* case the Court found that the new waiver was a notice of termination of the old unlimited waiver. It is true that the Board of Tax Appeals made this statement, but the Circuit Court did not base its affirmance on this ground, but rather on the ground that because the two instruments involved the same subject matter, the later one necessarily superseded the earlier one.

At page 13 of his brief, Appellee attempts to distinguish between a waiver providing for the "suspension" of the statute and one which provides a definite expiration date. It would seem that a reading of the statute should satisfactorily answer any argument the Appellee might make on this point. The applicable statute, Section 278(d) of the 1926 Revenue Act as Amended, provides for the "extension" of the statute by written agreement. In other places, Congress has used the word "suspension" as in Section 277 of the Internal Revenue Code, which provides that the statute shall be suspended pending an appeal to the Tax Court. The use of the two different words must have some significance. Hence, when a waiver, executed under Section 278(d), speaks of "suspending" the statute, its effect must necessarily be an "extension" of the statute since that is what the statute itself provides. As stated in *Wirt Franklin v. Commissioner*, 7 B. T. A. 636, at 639:

"The instrument under consideration is denominated an 'income and profits-tax waiver.' It is in fact a bilateral undertaking entered into by the parties pursuant to the statute. Technically, it is not a waiver of the statute, for it is made pursuant to the statute. It is not an acknowledgment of any existing obligation or a new promise to pay, from which a new cause of action arises, thus beginning anew the period of limitation. It is not an agreement not to plead the statute of limitations as a defense to any asserted tax liability. In short, it is not something to be considered as in avoidance of the statute. By the statute and by its terms, it operates to extend the time."

The case of *United States v. Fischer*, 93 F. 2d 488, cited at page 13 of Appellee's brief, has already been commented upon in Appellant's opening brief at pages 21 and 22 and no further comment is deemed necessary.

It is rather hard to understand the argument advanced by Appellee at pages 14 and 15 of his brief to the effect that the 1936 waiver was void because of a mutual mistake of fact or law. In the first place, the record shows that both parties were fully aware that the unlimited waiver was outstanding at the time the limited waiver was executed, and that the status of the unlimited waiver was uncertain. Hence, they must have intended the limited waiver to supersede it and settle all doubts as to the expiration of the statute. In the second place, any mistake there may have been is based upon an assumption that the unlimited waiver was invalid. If it was invalid, then the Appellant is entitled to a reversal of the lower Court's judgment without further ado.

If the unlimited waiver was not invalid, then it was, of course, no "mistake" on the part of either party when the subsequent limited waiver was filed.

The Appellee concludes his brief on page 18 with the citation of three cases in support of the proposition that suits for refund of taxes are governed by equitable principles. It should be noted first that the cases cited involve special situations and second, that equitable principles can hardly be applicable to a situation where the statute says in plain language that taxes paid after the expiration of the period of limitations on collection constitute an overpayment and shall be refunded.

Conclusion.

For the reasons stated in Appellant's opening brief, it is respectfully submitted that the judgment of the District Court should be reversed.

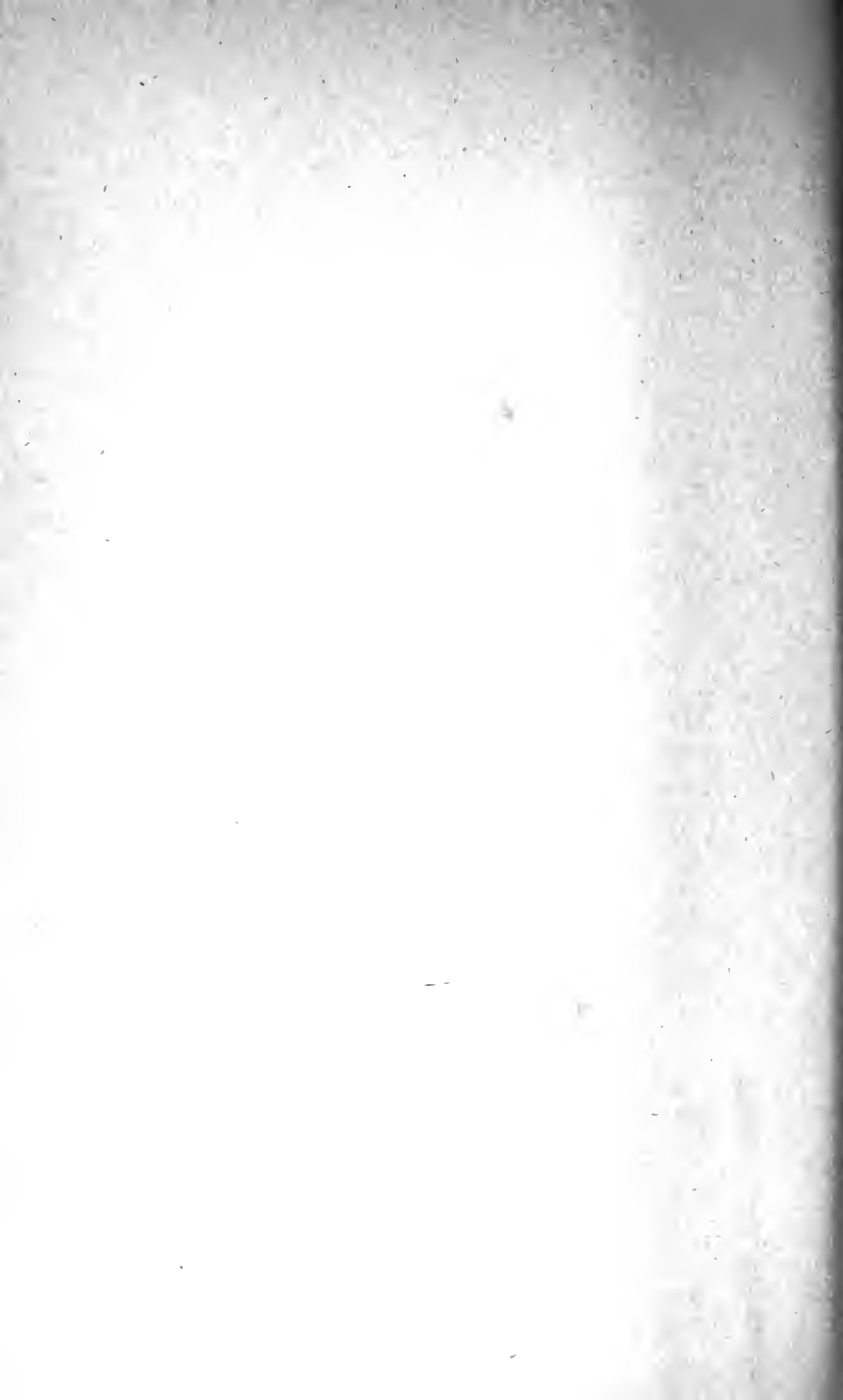
Respectfully submitted,

LATHAM & WATKINS,

By DANA LATHAM,

HENRY C. DIEHL,

Attorneys for Appellant.



No. 11974

United States
Court of Appeals
for the Ninth Circuit

WALLACE RAYMOND SHAVER,
Appellant,
vs.
UNITED STATES OF AMERICA,
Appellee.

Transcript of Record

Appeal from the District Court of the United States
for the Northern District of California,
Southern Division

NOV 1 - 1948

PAUL P. O'BRIEN,
CLERK



No. 11974

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Court of Appeals
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF ATTORNEYS

JAMES T. DAVIS,

1095 Market Street,
San Francisco, California,

Attorney for Defendant and Appellant.

FRANK J. HENNESSY,

United States Attorney,
Northern District of California,
Post Office Building,
San Francisco, California,

Attorney for Plaintiff and Appellee.

In the Southern Division of the United States
District Court for the Northern District
of California

No. 31417R

Viol, Title 18 United States

Code, Section 409

UNITED STATES OF AMERICA,

Plaintiff,

vs.

WALLACE RAYMOND SHAVER,

Defendant.

INDICTMENT

FIRST COUNT:

The Grand Jury charges: that

On or about the 30th day of October, 1947, at the City and County of San Francisco, State and Northern District of California, Wallace Raymond Shaver (hereinafter called "said defendant"), being an employee of a carrier, to-wit, Railway Express Agency, riding upon a motor truck of such carrier, transporting property in interstate commerce and having in his custody funds arising out of and accruing from such transportation, did embezzle and unlawfully convert to his own use, a portion of such funds, to-wit, the sum of \$73.29, which arose out of and accrued from an interstate

shipment of property from the City of Omaha, Nebraska, to and into the City and County of San Francisco, State of California. [1*]

SECOND COUNT:

The Grand Jury further charges: that

On or about the 4th day of September, 1947, at the City and County of San Francisco, State and Northern District of California, the said defendant, being an employee of a carrier, to-wit, Railway Express Agency, riding upon a motor truck of such carrier, transporting property in interstate commerce and having in his custody funds arising out of and accruing from such transportation, did embezzle and unlawfully convert to his own use, a portion of such funds, to-wit, the sum of \$18.25, which arose out of and accrued from an interstate shipment of property from LaGrange, State of Illinois, to and into the City and County of San Francisco, State of California.

A True Bill.

ARTHUR C. GRIFFIN,
Foreman, Deputy.

/s/ FRANK J. HENNESSY,
United States Attorney.

(Approved as to Form: R. B. McM).

[Endorsed]: Presented in open court and ordered filed May 12, 1948. [2]

*Page numbering appearing at foot of page of original certified Transcript of Record.

District Court of the United States, Northern
District of California, Southern Division

At a stated term of the District Court of the United States for the Northern District of California, Southern Division, held at the Court Room thereof, in the City and County of San Francisco, on Thursday, the 13th day of May, in the year of our Lord one thousand nine hundred and forty-eight.

Present: The Honorable Michael J. Roche,
District Judge.

[Title of Cause.]

ARRAIGNMENT

In this case the defendant, Wallace Raymond Shaver, was present in the custody of the United States Marshal and with his attorney, James Davis, Esq. Daniel C. Deasy, Esq., Assistant United States Attorney, was present on behalf of the United States.

On motion of Mr. Deasy, the defendant was called for arraignment. The defendant was informed as to the return of the Indictment by the United States Grand Jury, and asked if he was the person named therein, and upon his answer that he was and that his true name was Wallace Raymond Shaver, thereupon Mr. Davis waived the reading of the Indictment. Copy of Indictment was handed to the defendant, who stated that he understood the charge against him.

On motion of Mr. Davis and with consent of Mr. Deasy, it is ordered that the amount of bail for release of defendant be reduced from \$1000.00 to \$500.00.

Ordered that this case be continued to May 20, 1948, for entry of plea; and that in default of bail defendant be remanded to the custody of the United States Marshal. [3]

District Court of the United States, Northern
District of California, Southern Division

At a Stated Term of the District Court of the United States for the Northern District of California, Southern Division, held at the Court Room thereof, in the City and County of San Francisco, on Friday, the 28th day of May, in the year of our Lord one thousand nine hundred and forty-eight.

Present: The Honorable Michael J. Roche,
District Judge.

[Title of Cause.]

PLEA OF NOT GUILTY

This case came on regularly this day for entry of plea of defendant, Wallace Raymond Shaver, who was present in proper person and with his attorney, James Davis, Esq. E. H. Henes, Esq., Assistant United States Attorney, was present on behalf of the United States.

The defendant was called to plead and thereupon said defendant pleaded "Not Guilty" to the Indict-

ment filed herein against him, which said plea was ordered entered.

With the approval of the Court and the consent of the Government, the defendant waived trial by jury in writing.

After hearing counsel, it is Ordered that this case be continued to June 10, 1948, for trial. (Court.)

[Title of District Court and Cause.]

WAIVER OF JURY TRIAL

In conformity with Rule 23 of the Rules of Criminal Procedure for the District Courts of the United States, effective March 21, 1946, we, the undersigned, do hereby waive trial by jury and request that the above entitled cause be tried before the Court sitting without a jury.

Dated San Francisco, California, May 28, 1948.

WALLACE R. SHAVER,

Defendant.

JAMES T. DAVIS,

Attorney for Defendant.

E. HUGH HENES,

Assistant United States

Attorney.

Approved:

MICHAEL J. ROCHE,

Judge, United States District Court, Northern District of California.

[Endorsed]: Filed May 28, 1948. [5]

District Court of the United States, Northern
District of California, Southern Division

At a Stated Term of the District Court of the United States for the Northern District of California, Southern Division, held at the Court Room thereof, in the City and County of San Francisco, on Friday, the 11th day of June, in the year of our Lord one thousand nine hundred and forty-eight.

Present: The Honorable Michael J. Roche,
District Judge.

[Title of Cause.]

MINUTES OF TRIAL

This case came on regularly this day for trial before the Court sitting without a jury, a trial by jury having been heretofore waived. The defendant, Wallace Raymond Shaver, was present with his attorney, James Davis, Esq. Daniel C. Deasy, Esq., Assistant United States Attorney, was present on behalf of the United States. Mr. Davis made a motion to quash the Indictment, which motion, after hearing the arguments of counsel, was ordered denied. R. H. Rundle and Sam Papich were sworn and testified on behalf of the United States. Mr. Deasy introduced in evidence and filed U. S. Exhibits Nos. 1, 2, 3, 4, 6; and offered another exhibit which was marked U. S. Exhibit No. 5 for identification. The United States then rested. Both sides thereupon rested.

Mr. Davis made a motion for judgment of Not Guilty, which motion was ordered denied.

The case was submitted to the Court, and due consideration having been thereon had, it is Ordered that the defendant Wallace Raymond Shaver be, and he is hereby, Adjudged Guilty [6] as charged in the Indictment.

On motion of Mr. Davis, it is Ordered that this case be referred to the Probation Officer for investigation and report.

Ordered case continued to June 18, 1948, for pronouncing of judgment. Ordered that the defendant be remanded to the custody of the United States Marshal pending judgment.

Further ordered that U. S. Exhibit No. 5 for identification may be withdrawn. [7]

District Court of the United States, Northern
District of California, Southern Division

At a Stated Term of the Southern Division of the United States District Court for the Northern District of California, held at the Court Room thereof, in the City and County of San Francisco, on Friday, the 2nd day of July, in the year of our Lord one thousand nine hundred and forty-eight.

Present: The Honorable Michael J. Roche,
District Judge.

No. 31417-R

UNITED STATES OF AMERICA,

vs.

WALLACE RAYMOND SHAVER

It Is Ordered that the above named defendant be placed on Probation for the Period of Five (5) Years, one of the conditions of his probation be-

ing that defendant make restitution of the amount of money involved herein.

It Is Further Ordered that said defendant be released into custody of Charles H. Upton, Probation Officer of this Court, that defendant report to said Probation Officer as often and in such manner as directed, and further comply with all proper terms and regulations prescribed by said Probation Officer during the probationary period.

It Is Further Ordered that the matter of the pronouncing of judgment be suspended.

J. C. Astredo, Probation Officer, was present.

JAMES DAVIS,

Attorney for Defendant.

DANIEL C. DEASY,

Assistant U. S. Attorney. [8]

[Title of District Court and Cause.]

NOTICE OF APPEAL

Name and address of Appellant: Wallace Raymond Shaver, 211 "D" Street, San Rafael, California.

Name and address of Appellant's Attorney: James T. Davis, 1095 Market Street, San Francisco 3, California.

Offense: Violation of Title 18 United States Code, Section 409.

After trial by the Court a verdict was returned finding the defendant guilty on both counts of said indictment on the 11th day of June, 1948.

That thereupon, on the said 11th day of June,

1948, the defendant made a motion for a new trial, which motion was denied, and the Court thereupon referred the defendant to the probation officer and continued the matter of judgment.

That on the 2nd day of July, 1948, the Court made its judgment and sentenced the defendant as follows: Five Years Probation.

That defendant appeals from judgment of conviction and from the order denying his motion for a new trial.

Dated July 7, 1948.

JAMES T. DAVIS,
Attorney for Defendant.

Service of Copy of the foregoing Notice of Appeal admitted this 7th day of July, 1948.

FRANK J. HENNESSY,
United States Attorney.

[Endorsed]: Filed July 7, 1948.

[Title of District Court and Cause.]

DESIGNATION OF PARTS OF THE RECORD
DESIRED FOR USE IN APPEAL

The appellant designates the following as the Parts of the Record desired for use on appeal:

Indictment.

Plea of Not Guilty.

Reporter's Transcript.

Judgment.

Minutes of the Trial of June 11, 1948.

STATEMENT OF POINTS UPON WHICH
APPELLANT INTENDS TO RELY UPON
APPEAL:

Appellant intends to rely upon the following points upon appeal:

1. That the evidence was and is insufficient to support the verdict of guilty.
2. That the Court erred in denying appellant's motion to quash indictment.
3. That the Court erred in denying appellant's motion for a judgment of acquittal.

JAMES T. DAVIS,
Attorney for Appellant.

(Acknowledgment of Receipt of Copy.)

[Endorsed]: Filed Aug. 4, 1948. [10]

[Title of District Court and Cause.]

ORDER EXTENDING TIME TO FILE
TRANSCRIPT OF RECORD

Good Cause Appearing Therefor:

It is hereby ordered that the time within which appellant may file the Transcript of Record herein is hereby extended to and including the 27th day of September, 1948.

Dated this 4th day of August, 1948.

MICHAEL J. ROCHE,
Judge of the District Court.

[Endorsed]: Filed Aug. 4, 1948. [11]

[Title of District Court and Cause.]

**ORDER EXTENDING TIME TO FILE
TRANSCRIPT OF RECORD**

Good cause appearing therefor:

It is hereby ordered that the time within which appellant may file the Transcript of Record herein is hereby extended to and including the 5th day of October, 1948.

Dated this 20th day of September, 1948.

LOUIS E. GOODMAN,
Judge of the District Court.

[Endorsed]: Filed Sept. 20, 1948.

[12]

District Court of the United States, Northern
District of California

CERTIFICATE OF CLERK

I, C. W. Calbreath, Clerk of the District Court of the United States, for the Northern District of California, do hereby certify that the foregoing 12 pages, numbered from 1 to 12, inclusive, contain a full, true, and correct transcript of the records and proceedings in the case of United States of America, Plaintiff vs. Wallace Raymond Shaver, Defendant, No. 31417-R, as the same now remain on file and of record in my office.

I further certify that the cost of preparing and certifying the foregoing transcript of record on appeal is the sum of \$4.20 and that the said amount

has been paid to me by the Attorney for the appellant herein.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court at San Francisco, California, this 1st day of October, A. D. 1948.

(Seal)

C. W. CALBREATH,
Clerk.

[13]

In the Southern Division of the United States
District Court for the Northern Division
of California

Before Michael J. Roche, Judge.

No. 31417-R

UNITED STATES OF AMERICA,

Plaintiff,

vs.

WALLACE RAYMOND SHAVER,

Defendant.

REPORTER'S TRANSCRIPT

Friday, June 11, 1948

Appearances: For the United States: Daniel C. Deasy, Esq., Assistant United States Attorney. For the Defendant: James T. Davis, Esq. [1*]

The Clerk: U. S. vs. Shaver.

Mr. Deasy: Ready for the Government.

* Page numbering appearing at foot of page of original certified Reporter's Transcript.

Mr. Davis: Ready, Your Honor.

The Court: Now, how much time do you wish, counsel?

Mr. Davis: I don't think it will take more than half an hour.

Mr. Deasy: I don't think it will.

The Court: Under that statement, I will hold you to half an hour. You may proceed.

Mr. Davis: Thank you, Your Honor. In the first place, I would like to apologize for not being present yesterday.

The Court: Well, I got a report from the Clerk that cleared the matter up, so you needn't apologize to the Court at this time.

Mr. Davis: Thank you, Your Honor.

I wish to make this opening statement, if the Court please: There is no dispute as to the facts in this case whatsoever. However, this indictment is the document which has been returned, is the first one of its kind in this District. It has been brought under an amendment to the Code which was passed in 1946. As far as I know, it has not been passed upon, except in one case in the Southern District of California. As I say, there is no dispute as to the facts. However, I felt that in good conscience, I had to advise my client that in my opinion there is a serious question of law involved, and inasmuch as it [2] is a felony, I have to call to his attention that fact and determine whether or not he should enter a plea of guilty. Now at this moment, for the purposes of the record, I believe I should make a motion to quash the indictment on

the grounds that it does not state a public offense, does not state an offense against the United States of America, on the ground that the section involved reads in part as follows:

“Whoever shall * * * being an employee of any carrier riding in, on or upon any railroad car, motor truck, steamboat, vessel, aircraft, or other vehicle of such carrier transporting passengers or property in interstate or foreign commerce and having in his custody funds arising out of or accruing from such transportation, embezzle or unlawfully convert to his own use any such funds; * * *”

shall be punished as the law provides.

In other words, the point of my objection is this: I believe that that particular amendment which was passed, as I say, in 1946, and the previous one—there are two amendments—I believe were passed for the purpose of controlling actual interstate transportation, or the carriers, while they were actually engaged in the interstate transportation itself.

Now, as Your Honor is well aware, under the old statute prior to these amendments, which is still the law, the property itself has been held to be in interstate commerce from the time [3] it leaves the hands of the consignor until it arrives in the hands of the consignee. That is the property itself. However, I believe that these amendments are distinguished as to property, I believe that they specifically cover only the carrier itself, when the carrier is moving in interstate commerce. In other

words, there is one case, *Stone vs. the United States*, in 153 Fed. 2d 331, which controls amendment No. 4; and in that case the facts were that the defendants were dining car stewards who, while a train which was itself moving in interstate commerce, defrauded the railroad company of meal checks by a trick and device with service men, whereby they could cancel one check and not turn the other one in.

Now, frankly, I don't know about this second section, Section 5—the second amendment—which, as I say, reads as follows:

“Whoever shall * * * being an employee of any carrier riding in, on or upon any railroad car, motor truck, steamboat, vessel, aircraft, or other vehicle of such carrier transporting passengers or property in interstate or foreign commerce and having in his custody funds arising out of or accruing from such transportation, embezzle or unlawfully convert to his own use any such funds; * * *”

shall be punished as the law provides. Now, I think as the facts will indicate, Your Honor, this man was a driver for the American Railway Express. His truck, I believe, admittedly did [4] not leave the city and county of San Francisco. He handled local freight, interstate freight and intrastate freight. There is no doubt about it. There is no question, and the man so admits, that on two counts, the facts upon which the two counts of the indictment are based, that he did have on his truck two shipments of interstate freight and that he de-

livered those to the consignees and collected the money, the C.O.D. and freight charges, and did not turn it in to the Company.

However, Your Honor, I am not satisfied—although I admit those facts—that he has violated the law or that his actions constitute an offense against the United States. That is why I raise the point.

The Court: Very well. I will hear from the Government.

Mr. Deasy: As Mr. Davis has advised Your Honor, this indictment is based upon the 1946 amendment to the statute, which added two new portions, enlarging the classes of acts made criminal by the statute. They added Section 4, which makes it an offense to:

“* * * embezzle, steal or unlawfully take by any fraudulent device, scheme or game, from any railroad car, motor truck, steamboat, vessel, aircraft, or other vehicle operated by any carrier, or from any passenger or employee thereon, when such railroad car or the train of which it is a part, motor truck, steamboat, vessel, aircraft, or other vehicle is moving in interstate or foreign commerce, any [5] money, baggage, goods, or property, with intent to convert the same or any part thereof to his own use, or shall buy, receive, or have in his possession any such money, baggage, goods or property, * * *”

Section 5, the one under which this indictment in this case is laid, reads:

“Whoever shall * * * being an employee of any carrier riding in, on or upon any railroad car, motor truck, steamboat, vessel, aircraft or other vehicle of such carrier transporting such passengers or property in interstate or foreign commerce and having in his custody funds arising out of or accruing from such transportation, embezzle or unlawfully convert to his own use any such funds; * * *”

Now, the Government's position is that the wording of the statute does not limit the cases to those where the truck itself actually moved from state to state, but that it applies to any employee “of any carrier riding in * * * any * * * motor truck * * * transporting * * * property in interstate or foreign commerce and having in his custody funds arising out of * * * such transportation,” which is the case here.

As I view it, the American Railway Express Agency is a carrier in the sense that it picks up and ships, forwards and delivers freight both interstate and intrastate. The shipments involved here came, one of them, from Omaha, Nebraska and the [6] other from LaGrange, Illinois. Both of them were subject to having charges collected upon delivery. The defendant in the case was, as is stated in the indictment, an employee of the Railway Express Agency, and while riding on their truck belonging to the Railway Express Agency, driving the truck, embezzled and converted to his own use funds arising from the transportation. By that I mean funds the collection of which had

been effected by him from the consignees of the goods which had come from, in one case, Omaha, and in the other, LaGrange, Illinois.

Mr. Davis's point is simply this: Does the statute require that the motor truck should actually move, physically move, the goods from one state to another, or, in other words, does it cover such a situation as is charged in the indictment in this case, where the goods were brought in and then placed upon the truck in San Francisco for ultimate completion of the delivery? I feel that the statute covers the situation we have charged in the indictment in this case. It isn't necessary under the statute that the motor truck on which defendant was riding at the time of this embezzlement should be a truck that actually, physically perhaps, transported the goods from some other state into California. It merely completes the shipment. As Your Honor knows, in these interstate shipments they go through many hands between the consignor and the consignee. That was the case here. The goods were picked up by the [7] Railway Express Agency at the point of shipment and were transported by means of railroad cars or otherwise into California, where the ultimate completion of delivery was to be made by the motor truck on which this defendant was the driver. I feel that it is covered by the statute, that the indictment charges the offense under the statute properly.

The Court: It is my thought that the law as amended covers the factual situation in this case. However, I want you to save, for the purpose of

the record, any legal point that you desire to raise hereafter.

Mr. Davis: Yes, Your Honor.

The Court: You want to develop the factual situation now?

Mr. Davis: Yes. Then the motion to quash is denied?

The Court: The motion to quash will have to be denied. Call your first witness.

Mr. Deasy: Mr. Rundle.

R. H. RUNDLE

called as a witness on behalf of the United States, sworn.

The Clerk: Q. Will you state your name?

A. R. H. Rundle.

Direct Examination

Mr. Deasy: Q. What is your occupation, Mr. Rundle?

A. Special agent, Railway Express Agency.

Q. Did you bring with you to court this morning certain [8] documents pertaining to a shipment from Omaha, Nebraska to California, during the month of October of 1947, and the documents pertaining to a shipment from LaGrange, Illinois, to San Francisco during the month of September of 1947?

A. Yes, I have those documents here.

Q. May I see them, please?

A. You want me to explain them to you?

Q. Let me have them first.

The Court: You are familiar with these documents, counsel?

(Testimony of R. H. Rundle.)

Mr. Davis: No, I haven't seen them.

Mr. Deasy: I don't know whether you have seen them; those are the receipts.

Mr. Deasy: Q. Now, Mr. Rundle, I will show you these documents that you have handed me. What is this first one I am showing you here?

A. That is the customer's receipt, back in Omaha, that we issue when we pick up the shipment or when the shipment first comes into our possession. We issue this receipt with a contract attached showing that we will deliver this shipment as addressed in San Francisco.

Q. And from whom did you obtain that?

A. From Cornelia Erdman, Bekins Van & Storage Company.

The Court: In the interest of time, show him the other documents. [9]

Mr. Deasy: Yes, Your Honor.

Mr. Deasy: Q. And this is a similar one on another shipment, is it?

A. That is the same, a receipt issued at La-Grange, Illinois, to Mrs. Israel Smith, declaring that we will deliver that shipment in San Francisco.

Q. And what are these other two documents that you have shown me here?

A. These are receipts issued by the driver upon delivery of these shipments, signed with his initials, and indicated that the money is collected and how much.

Mr. Deasy: Now, the first document handed to me shows—

(Testimony of R. H. Rundle.)

The Court: The witness on the stand probably will recite that better, counsel; he is familiar with them.

Mr. Deasy: I just wanted to state to Your Honor that it shows the destination office as San Francisco, California, the consignee as Cornelia Erdman, c/o Bekins Van & Storage, at 13th and Mission Street. The name of the forwarding office is Omaha, Nebraska, and the name of the shipper is also Cornelia Erdman, the street address being Bekins Van & Storage, 16th and Leavenworth; it covers seven pieces of H. H. goods. This is a receipt numbered 4844.

The Court: Very well.

Mr. Deasy: I ask that be marked.

The Court: It may be admitted and marked. Any objection? [10]

Mr. Davis: No objection.

The Clerk: No. 1.

(Railway Express Agency receipt No. 4844, referred to above, was thereupon received in evidence and marked United States Exhibit No. 1.)

Mr. Deasy: And I have a similar document, which is marked as receipt No. 2025, showing the destination office as San Francisco, California, the consignee as Mrs. Israel Smith, 9 Castle Manor, LaGrange, Illinois; the name of the forwarding office is LaGrange, Illinois, the name of the shipper is the Jackson Storage & Van Company, and the shipping consists of one box hair dryer, and ask that that be admitted also.

(Testimony of R. H. Rundle.)

The Court: It may be admitted next in order.

The Clerk: No. 2.

(Railway Express receipt No. 2025 was thereupon received in evidence and marked United States Exhibit No. 2.)

Mr. Deasy: The next document is a document entitled "Receipt for Charges collected from Consignee, San Francisco, Calif," dated—it appears to be 10/3/194... It is made out to Bekins in pencil and in ink to Cornelia Erdman, showing the shipper as being "Do318/15," the address as Omaha, Nebraska. It is marked "Paid," with the initials "W.R.S.," showing the total amount of \$73.29.

The Court: It may be admitted and marked.

The Clerk: No. 3. [11]

(Railway Express receipt referred to was thereupon received in evidence and marked United States Exhibit No. 3.)

Mr. Deasy: The next document is a document marked "Consignee's Receipt for Charges," made out "To Destination Office, San Francisco, Calif., Consignee, Mrs. Israel Smith, 90 Castle Manor Avenue," with the name of the forwarding office as LaGrange, Illinois. The shipper is shown as Jackson Storage & Van Company. It is marked "Paid, W.R.S.," showing a total amount of \$18.25, and this is dated "8-27—"—and I can't read the rest. It is "8-2," and something that looks like "74."

The Court: It may be admitted next in order.

The Clerk: No. 4.

(Testimony of R. H. Rundle.)

(Railway Express receipt referred to was thereupon received in evidence and marked United States Exhibit No. 4.)

Mr. Deasy: Q. Now the last two documents that you handed me, Government's Exhibits No. 3 and 4, the two receipts, did you at any time exhibit those to the defendant Shaver in this case?

A. Yes, I have.

The Court: Q. Where and under what circumstances?

A. Well, we took a statement from him in our office, my office at Pier 14.

Q. When? Fix the time.

A. April 7—no, April the 8th. [12]

Q. What time of the day was it?

A. Well, it was approximately—we had been there all day. It was approximately 10:00 o'clock in the morning, I would say.

Q. Who was present?

A. Special agent E. W. Hogan and myself.

Q. State what occurred.

A. And the defendant.

Q. State what occurred.

A. Well, we brought Mr. Shaver in to question him about this here case, and finally Mr. Shaver admitted it, and we took a statement from him to this effect on that date.

Q. Have you got that statement?

A. Yes, I have.

The Court: Have you seen this statement, counsel?

(Testimony of R. H. Rundle.)

Mr. Davis: No, I haven't.

Mr. Deasy: I haven't seen it either, Your Honor.

The Court: You may examine it.

Mr. Deasy: A later statement, I might advise the Court, was taken by Mr. Patrick of the FBI, which I intended to bring out.

The Court: Is he here?

The Witness: Yes, sir.

The Court: Very well.

Mr. Deasy: At this time I was simply questioning this witness as to whether he had at any date exhibited these two [13] documents to Mr. Shaver.

The Court: You may ask him.

Mr. Davis: I have seen the statement of the FBI agent, Your Honor, but not this statement.

Mr. Deasy: I haven't seen it myself; it is rather lengthy, Your Honor.

The Witness: I think it is eight or nine pages.

The Court: Mark it for purposes of identification, if there is any question about it.

Mr. Davis: I have no objection to it being marked for identification.

The Court: It may be admitted and marked for purposes of identification.

Mr. Deasy: This is a portion of the witness' files. There is another whole file. Will you take this—

The Court: Well, you can leave it on. Maybe there will be no necessity for it. Just leave it on there.

(Testimony of R. H. Rundle.)

The Clerk: No. 5 for identification.

(Statement of defendant referred to was thereupon marked United States Exhibit No. 5 for identification.)

Mr. Deasy: Q. Now, did you on the occasion just referred to exhibit these two documents, Government's Exhibits No. 3 and 4 to Mr. Shaver?

A. That is the last two documents you are speaking of?

Q. These are the two. [14]

A. The two consignee receipts? What was your question?

Q. Did you on that date show these to Mr. Shaver? A. Yes.

Q. And did you question him concerning the handwriting or initials appearing on these documents?

A. That's right. He admitted they were his initials.

Q. His initials, "W.R.S."?

A. That's right.

Q. Did he tell you whether or not he had marked them "Paid"?

A. He admitted that he collected the money and did not turn it in, if that is what you mean.

Q. And he told you that the writing "Paid, W.R.S." was written on there by him, is that right? A. Yes.

Q. What was Mr. Shaver's employment at that time? A. He was a driver.

Q. A truck driver? A. Truck driver.

(Testimony of R. H. Rundle.)

Q. For the American Railway Express Agency?

A. That's correct.

Mr. Deasy: No further questions.

The Court: You may take the witness, counsel.

Cross Examination

Mr. Davis: Q. Mr. Rundle, the defendant, Mr. Shaver, is an employee of the Railway Express Agency, is that correct? [15] A. He was.

Q. He was? A. Yes.

Q. And on the date named in the indictment he was an employee, is that correct?

A. No, I believe when he was indicted, I believe—it is in the file there when we took his resignation. I believe he resigned on the 8th of April; I am not too sure to that. I would have to refer to my file.

Q. You probably didn't understand my question, Mr. Rundle. On the 30th day of October, 1947, was he an employee of the Railway Express?

A. That's right, he was an employee.

Q. And on the 4th day of September 1947 was he an employee? A. Yes, he was.

Q. Now, the Railway Express Agency is in the business of transporting freight, is that correct?

A. That's correct, and express.

Q. And Mr. Shaver, I take it, was, on those two dates one of your truck drivers, is that correct? A. That's correct.

Q. What was his route in driving his truck?

A. He had what we would call a "special route," south of Market Street; in other words, he

(Testimony of R. H. Rundle.)

would cover from the Embarcadero all the way to the Beach. [16]

Q. Confined to the City and County of San Francisco? A. That's right.

Q. He never drove his truck outside of the City and County of San Francisco, is that correct?

A. I am not too sure about that; I can't answer that question. He may have went to San Rafael on occasion, and he might have went to San Pablo on occasion.

Q. Well, in any event, he didn't drive his truck outside of the State of California?

A. No, he did not.

Q. And on his truck, what types of freight did he handle? If I may explain that, rather than a description, please state whether he handled interstate, intrastate or local freight, or what.

A. He went out with both kinds. He would have interstate and intrastate.

Q. Any local freight? A. He could have.

Q. Could have?

A. Very little. We have been having very little of that.

Q. And he drove from the railroad yards usually to the various consignees, is that correct?

A. That's right.

Q. And made individual deliveries? [17]

Mr. Davis: That is all.

Redirect Examination

Mr. Deasy: Q. Do you know, Mr. Rundle, how and by what means the shipments covered by these

(Testimony of R. H. Rundle.)

documents which you have produced arrived at San Francisco?

A. By train or—to San Francisco?

Q. Correct.

A. They arrived at Oakland Pier by train and ferried across on the boat to our Pier 14, San Francisco.

Q. In other words, they came in from Omaha and LaGrange, respectively, by railroad train?

A. That's right.

Q. And the terminus is at Oakland; that is the terminus of the trains, at Oakland, and it is then loaded onto the ferryboat to be brought to San Francisco?

A. That's right.

Q. And you took possession, then, in San Francisco, is that right?

A. That's right.

Q. And they were there loaded on trucks to be delivered to the consignees?

A. And they were sorted on our platform and divided into different groups of the city, and Mr. Shaver, of course, had his own particular route, a section of the city, and he would load his own trucks. [18]

Q. Now, calling your attention to Government's Exhibit No. 3, can you explain whether this called for the collection of some funds by the driver in connection with that shipment, is that right?

A. That's correct.

Q. And those charges are enumerated on the document here, is that true?

A. That's right.

(Testimony of R. H. Rundle.)

Q. And they cover value charges of 90 cents, express charges of \$63.25, tax of \$1.92, that is totaled at \$66.07; C.O.D. charges of \$6.94, C.O.D. service charge of 28 cents, to make a grand total of \$73.29, is that correct? A. That's right.

Q. Was the amount to be collected by the driver, and does this document purport to show that it has been collected? Is that right?

A. That is correct.

Q. Now, calling your attention to Government's Exhibit No. 4, this shows, does it, the amount of charges to be collected by the driver in this receipt?

A. Yes, it does.

Q. And they call for express charges of \$11.73, tax of 35 cents, to make a total of \$12.07; added are C.O.D. charges of \$5.90, C.O.D. service charges of 28 cents, to make a grand total of \$18.25, is that right? [19] A. That's correct.

Q. And this receipt purports to show that it has been collected by the driver?

A. That's correct.

Mr. Deasy: No further questions.

Recross Examination

Mr. Davis: Q. Mr. Rundle, you are familiar with the records kept in the regular course of business of the Railway Express Agency, are you not?

A. Yes, I am.

Q. And from examining Government's Exhibits 1, 2, 3 and 4, can you state from those records that these two deliveries came from the towns in question. Omaha and LaGrange?

(Testimony of R. H. Rundle.)

A. Yes; you see, in order for the defendant to write that receipt, he would have to have a delivery sheet, and on that delivery sheet is the same number that is on this folding receipt, so if you will notice on these exhibits here, you will see that the delivery receipt on this one, No. 4844, shows on this original receipt that I have obtained from Omaha, which we issued at Omaha, and it carries that same number.

Q. I see. In other words, when you testify that these two deliveries arrived here by train into Oakland and then were ferried across the Bay, are you testifying of your own knowledge or from these documents that you have looked at?

A. Well, from the documents, of course. I haven't seen the [20] shipments.

Mr. Davis: I have no further questions.

The Court: Step down.

Call your next witness.

SAM PAPICH

called as a witness on behalf of the Government,
sworn.

The Clerk: Q. Will you state your name?

A. Sam Papich.

Direct Examination

Mr. Deasy: Q. And your occupation, Mr. Papich?

A. I am a special agent of the FBI.

Q. Do you know the defendant in this case, Mr. Wallace Raymond Shaver? A. I do, sir.

(Testimony of Sam Papich.)

Q. And did you ever have a conversation with him concerning the matters which are charged in this indictment?

A. I had a conversation with him on April 14, 1948, in his apartment on 101 Parnassus Avenue.

Q. And were any other persons present at that time?

A. A roommate, Clifford Piltz, was also present. That was about 10:00 o'clock in the morning.

Q. And at that time did you identify yourself to Mr. Shaver as an FBI agent?

A. I did, sir. [21]

Q. And what else, if anything, did you tell him at that time?

A. I advised Mr. Shaver that I wanted to question him regarding the matter of some shipments which he handled for the Railway Express Agency, and advised him that he had the right to legal counsel before making any statements. I also advised him that anything he might say would be held against him in a court of law. He subsequently furnished a voluntary statement to me.

Q. You had a conversation with him at that time, did you? A. Yes, sir.

Q. And from that conversation you prepared a written statement, did you? A. I did, sir.

Q. And did you exhibit that statement to Mr. Shaver? A. I did.

Q. And did he read it, do you know?

A. He did read it.

Q. And did you ask him to sign the statement?

A. I did.

(Testimony of Sam Papich.)

Q. And did he do so? A. He did, sir.

Q. Have you that with you?

A. Yes, I have it here, sir.

Mr. Deasy: Did you see this?

Mr. Davis: I saw the printed one, or the typed one. [22]

Mr. Deasy: Q. This statement was signed by Mr. Shaver in your presence, was it?

A. It was, sir.

Q. And in the presence of C. E. Piltz?

A. That's right, sir.

Q. And that is the man you referred to as his roommate? A. That's right.

Mr. Deasy: At this time I would like to offer it in evidence.

The Court: It may be admitted.

The Clerk: No. 6.

(The statement referred to above was received in evidence and marked United States Exhibit No. 6.)

Mr. Deasy: May I read it at this time:

“San Francisco, California. 4/14/48.

“I, Wallace Raymond Shaver, make the following voluntary statement to Sam Papich, who has identified himself to me as being a Special Agent of the Federal Bureau of Investigation. No threats or promises have been made to me. I have been advised that I can have legal counsel before making any statements. I know that anything that I say can be used against me in a court of law.

(Testimony of Sam Papich.)

"I am 39 years of age and a native of California. I have a high school education and I attended a teacher's college for one and a half years. I have been a truck [23] driver for the Railway Express Agency, San Francisco, for approximately two and a half years. I resigned April 7, 1948. On or about October 30, 1947, I delivered a shipment of seven pieces to the Bekins Van & Storage Co., San Francisco. I received about \$70.00 from Bekins which amount covered express charges, tax, value charges, and C.O.D. return charges. I gave Bekins a receipt and I did not settle this amount with the company. I kept the money for my own use. I recall that on the same day I made the delivery to Bekins I made a delivery of approximately twenty other shipments. I did not make settlements with the Railway Express Agency for the amounts collected on the deliveries. In addition to the \$70.00, I collected from Bekins, I believe I collected approximately \$80.00 from other deliveries, all of this on the same day. I kept this money for my own personal use.

"I recall that in the early part of September 1947, I made several deliveries of shipments in San Francisco. On this particular day I made several collections totalling to approximately \$150.00. I did not make settlements with the Railway Express Agency on these collections. I kept this money for my own personal use. On April 8, 1948, Special Agent E. W. Hogan of the Railway Express Agency showed me a receipt issued to a Mrs. Israel Smith, No. 9 Castle Manor, San Francisco, for a

(Testimony of Sam Papich.)

delivery of a shipment [24] from LaGrange, Illinois. I recognized my initials on this receipt indicating that I made the delivery and collected the charges. I believe it is one of the deliveries I made on the day in early September when I kept approximately \$150.00.

“I also recall that in early September, 1947, I made a delivery to a Mrs. Gordon on Aptos Way, San Francisco. I collected \$30.00 or \$40.00 on this delivery and I did not make a settlement with the Railway Express Agency. I kept the money for my own use.

“I wish to add that Special Agent E. W. Hogan showed me a receipt covering the delivery to Bekins Van & Storage Co. This receipt showed that shipment originated in Omaha, Nebraska. I recognized my initials on this receipt. These initials would have been made at the time of the collection for the delivery.

“At this time I wish to state that there is a possibility there may have (been) other instances when I made deliveries and kept the collections for my own use, but to my knowledge at present time, there were not any instances other than described above.

“I have read the above statement of two pages including this page and everything is true as well as I can recall.

“Wallace R. Shaver.

[25]

(Testimony of Sam Papich.)

“Witnesses:

“Clifford E. Piltz,
101 Parnassus, San Francisco.
“Sam Papich.
F.B.I., San Francisco.

4/13/48.”

Mr. Deasy: I have no further questions.

Cross Examination

Mr. Davis: Q. Mr. Papich, when you questioned Mr. Shaver, do you know whether any of these other transactions that he described were interstate shipments? Have you been able to trace any of these?

A. No, I have’nt, sir.

Q. So that out of the group that he described, the only two that you know of as being interstate are the two named in the indictment, is that correct? A. That’s right, sir.

Mr. Davis: That is all, sir.

The Court: Step down.

Mr. Deasy: We rest, Your Honor.

Mr. Davis: I have no witnesses, Your Honor, and I now wish to make a motion for a directed verdict of a judgment on the pleadings upon the same grounds that I made my motion to quash the indictment. In other words, Your Honor, I feel that under the previous law the Courts were very careful to distinguish or to point out that the goods stolen had to be stolen from some one of the specific places named in the indictment, [26] such as a wharf, a railroad car, a truck, and so forth. In

other words, it is jurisdictional as to whether or not the Federal Government has any control over this property unless it is actually moving in interstate commerce.

Now, my feeling is that if we are going to accept these amendments as extending the law to the facts as we hear them in this case, it is going to mean that the Federal Government has jurisdiction over practically every truck, streetcar or any other vehicle moving in a locality if it merely happens to handle a piece of interstate freight. In other words, I don't believe that the analogy would be strained to say that if a man got on a municipal railway car with a package of interstate freight to take it out to be delivered, that would in effect make the municipal railway streetcar an interstate carrier; and I don't think that Congress intended to go that far.

The Court: I quite agree with you, but we are here concerned with a man working for the Railway Express, who was engaged in that very activity.

Mr. Davis: That is true, Your Honor. However, they do handle both—they handle local, interstate and intrastate.

My only point is, Your Honor, that I feel in order to bring the case within this statute that the carrier itself has to be transporting passengers or property in interstate freight, and the fact that some property on a peculiarly local carrier happens to be interstate, I don't think brings it within this [27] classification.

The Court: I think the amendment covers it. The motion will have to be denied.

Do you want to submit the case?

Mr. Davis: Yes, sir, we will submit it at this time.

The Court: The Court will have to adjudge the defendant guilty as charged.

Mr. Davis: If the Court please, as you may have understood from me making these technical motions, I feel that in justice to my client, I should take this matter up on appeal. I think it should be decided one way or the other, inasmuch as it is the first case in this District. I would like to move at this time that the defendant be released on bail pending his appeal, because I feel that the defendant has admitted all of the facts. He has not denied any of them. It is really upon my advice that he is taking this technical move, as I feel he is justified to do, because if he is not guilty of this offense, I don't believe that he should have the stigma of having been found guilty or of pleading guilty to a felony charge.

The Court: Very well, I will assist you in any way I can so that there will be a final determination of this matter. What do you wish, to fix a bail on appeal?

Mr. Davis: Yes.

The Court: What is the bail?

Mr. Davis: The defendant is out on a \$500 bail now, Your [28] Honor.

The Court: Is there any objection to bail?

Mr. Deasy: No, Your Honor, there is no objection to continuing on bail.

The Court: He may remain on bail, and it will be fixed at \$500.

Mr. Davis: Thank you, Your Honor.

The Court: Very well.

Mr. Deasy: Do you want at this time to fix a date for judgment, Your Honor?

The Court: What day? What date for judgment?

Mr. Davis: What day do you want?

Mr. Deasy: Any time.

Mr. Davis: Any date is agreeable to me.

The Court: I will have to take the usual course and refer the matter, so that the Court can be properly advised, to the Probation Department for a pre-sentence report. The defendant will have to go into custody.

Mr. Davis: Might I suggest two weeks, Your Honor?

The Court: Very well, two weeks.

Mr. Davis: Your Honor, I thought that Your Honor had granted the motion to release the defendant on bail pending his appeal.

The Court: No, I will have to take the usual course; I had in mind that bail on appeal, but until I receive the pre-sentence [29] report—if it is agreeable to the Government, that thought was limited to bail for the purpose of appeal. Judgment hasn't been imposed yet.

Mr. Davis: I see, Your Honor.

The Court: And the Court wishes to be advised before sentence is imposed.

Mr. Davis: Might I suggest, then, Your Honor,

—I don't like to attempt to tell the Court that I am imposing upon your prerogatives—

The Court: No, we proceed here with a degree of liberty that is surprising at times, if the facts warrant it.

Mr. Davis: What I meant was this, Your Honor: Without trying to impose on the prerogatives of the Court, from the facts in the case, I believe that the defendant will appear to be, after investigation, a fit subject for probation. I have checked his background and I understand he has had no previous difficulty and never been in trouble before and that this is his first offense. Therefore I would suggest that if it is possible that the probationary period or the period for investigation be reduced to one week, rather than two weeks.

The Court: Very well, one week. The defendant may go into custody.

The Clerk: June 18.

[Endorsed]: Filed Sept. 22, 1948. [30]

[Endorsed]: No. 11974. United States Court of Appeals for the Ninth Circuit. Wallace Raymond Shaver, Appellant, vs. United States of America, Appellee. Transcript of Record. Appeal from the District Court of the United States for the Northern District of California, Southern Division.

Filed October 1, 1948.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for
the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 11974

WALLACE RAYMOND SHAVER,

Appellant,

vs.

UNITED STATES OF AMERICA,

Respondent.

STATEMENT OF POINTS UPON WHICH
APPELLANT INTENDS TO RELY AND
DESIGNATION OF PORTIONS OF THE
RECORD FOR THE CONSIDERATION
THEREOF

The Appellant adopts as his Statement of Points on Appeal the Statement of Points appearing in the certified typewritten Transcript of Record.

The Appellant designates for printing the entire certified typewritten Transcript of Record.

/s/ JAMES T. DAVIS,
Attorney for Appellant.

[Endorsed]: Filed October 14, 1948. Paul P. O'Brien, Clerk.

[Title of U. S. Court of Appeals and Cause.]

STIPULATION THAT PORTIONS OF THE
RECORD NEED NOT BE PRINTED

It Is Hereby Stipulated by and between the Appellant and Respondent, by their respective counsel, that Plaintiff's Exhibits I, II, III and IV need not be printed as part of the Record on Appeal, but may be considered in their original form and in such form may be considered a part of the Record on Appeal.

/s/ FRANK J. HENNESSY,
United States Attorney.

By /s/ DANIEL C. DEASY,
Assistant U. S. Attorney,
Attorneys for Respondent.

/s/ JAMES T. DAVIS,
Attorney for Appellant.

[Endorsed]: Filed October 14, 1948. Paul P. O'Brien, Clerk.

[Title of U. S. Court of Appeals and Cause.]

**ORDER THAT PORTIONS OF THE RECORD
NEED NOT BE PRINTED**

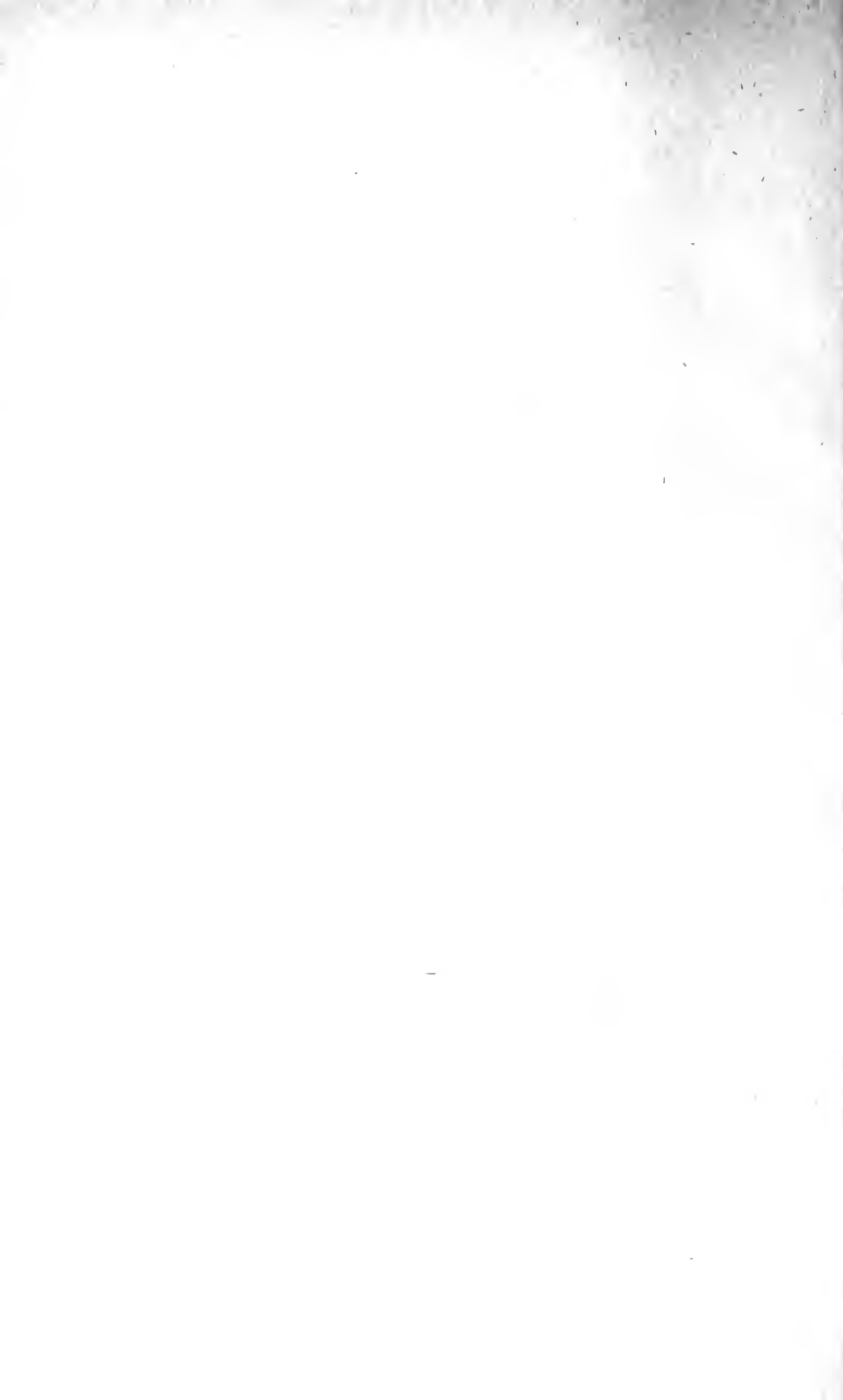
Good Cause Appearing Therefor and pursuant to the stipulation of the parties hereto, it is hereby ordered that Plaintiff's Exhibits I, II, III and IV need not be printed as part of the Record on Appeal, but may be considered in their original form and in such form shall be considered a part of the Record on Appeal.

/s/ WILLIAM DENMAN,
Chief Judge, United States Court of Appeals for
the Ninth Circuit.

[Endorsed]: Filed October 15, 1948. Paul P.
O'Brien, Clerk.







No. 11,974

IN THE

**United States Court of Appeals
For the Ninth Circuit**

WALLACE RAYMOND SHAVER,	}
vs.	
UNITED STATES OF AMERICA,	
	<i>Appellant,</i>
	<i>Appellee.</i>

APPELLANT'S OPENING BRIEF.

JAMES T. DAVIS,
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PAUL P. O'BRIEN,
CLERK

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No. 11,974

IN THE

**United States Court of Appeals
For the Ninth Circuit**

WALLACE RAYMOND SHAVER,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLANT'S OPENING BRIEF.

JURISDICTIONAL STATEMENT.

This is an appeal from the judgment of conviction (Tr. 8) of the District Court of the United States for the Northern District of California, Southern Division, convicting the defendant, after a trial by the Court, of a violation of 18 U.S.C. 409. The indictment (Tr. 2-3) was in two counts, charging in the first count, that the defendant, on or about the 30th day of October, 1947, in the City and County of San Francisco, State of California, being an employee of a carrier, to wit, Railway Express Agency, riding upon a motor truck of such carrier, transporting property in interstate commerce and having in his custody funds arising out of and accruing from such transportation, did embezzle and unlawfully convert to his

own use a portion of such funds, to wit, the sum of \$73.29 which arose out of and accrued from an interstate shipment of property from Omaha, Nebraska, to and into San Francisco, California.

In the second count, a similar offense was charged in identical language, except as to the date of the offense, the amount alleged to have been embezzled and the place of shipment.

The Court below had jurisdiction under the provisions of Title 28 U.S.C., Section 41, Subdivision 2. The jurisdiction of this Honorable Court is invoked under the provisions of Title 28 U.S.C., Section 225, Subdivisions (a) and (d).

STATEMENT OF FACTS.

There is no dispute as to the facts of this case. It is admitted that the defendant, on the dates named in the indictment, was an employee of the Railway Express Agency driving a truck in San Francisco and its environs hauling local, interstate and intrastate freight. While so employed, he did not drive the truck out of the State of California. On each of the occasions charged in the indictment the defendant delivered a package of interstate freight to the consignee, collected the amount due thereon (which consisted of taxes, express, service and C.O.D. charges) and failed to turn the amount so collected over to his employer.

STATEMENT OF POINTS RELIED ON.

Appellant relies upon the following point.

That the evidence was insufficient to support either the verdict of guilty or the judgment and sentence of the Court for the reason that, admitting all of the facts to be true, they do not constitute a violation of the statute in question.

ARGUMENT.

In 1946 Section 409 of Title 18 United States Code was redrafted.* The crime of embezzlement was added and the Section was divided into five paragraphs of which Paragraph 5 is new matter. The indictment in this case was brought under the provisions of said Paragraph 5 and, as far as we have been able to ascertain, this is a case of first impression. The indictment now before the Court is the first to be brought under said Paragraph 5 in this District.

Paragraph 5 reads as follows:

“being an employee of any carrier riding in, on or upon any railroad car, motortruck, steamboat, vessel, aircraft, or other vehicle of such carrier transporting passengers or property in interstate or foreign commerce and having in his custody funds arising out of or accruing from such transportation, embezzle or unlawfully convert to his own use any such funds;”

shall be found guilty of a felony.

*60 Stats. Pub. Law 534, Chap. 606.

It is the contention of the appellant that in order to constitute a violation of this paragraph the vehicle of the carrier upon which the defendant is riding as an employee must, at the time of the embezzlement, be moving in interstate or foreign commerce, and that it is not sufficient if, as in this case, the vehicle is a purely local one although the goods or the property being transported may be of an interstate or foreign character.

In the first place it is necessary to draw a distinction between the property being transported and the carrier transporting the same. Under the provisions of Paragraph 2 of Section 409 which covers the larceny of property from carriers engaged in interstate or foreign commerce it has been uniformly held that the property is in interstate commerce from the time it leaves the hands of the consignor until it reaches the hands of the consignee.

Boyd v. United States (C.C.A. 4), 275 Fed. 16;

Friedman v. United States (C.C.A. 1), 233 Fed. 429;

Sharp v. United States (C.C.A. 5), 280 Fed. 86.

The language of Paragraph 1, however, covers not only "goods or property moving as interstate or foreign commerce" but also "goods or property * * * which are a part of or which constitute an interstate or foreign shipment of freight or express."*

It does not follow, therefore, that because the goods or property are themselves in interstate commerce,

*18 U.S.C. 409, Par. 2.

that the carrier moving them at any particular time is moving in interstate commerce.

It is a common practice to ship small lots of goods to a carloading company at a central point for transshipment to their ultimate destination. The appellant contends, for example, that if a consignor ships goods from New York to Chicago for the purpose of having them loaded into a car with other goods for shipment to San Francisco and the goods are moved from one depot to another in Chicago, while the goods themselves are part of an interstate shipment, the carrier so moving them from one depot to another in Chicago is not moving in, or engaged in, interstate commerce.

Keeping in mind that the power of Congress to pass legislation of this type comes from the Commerce Clause of the Constitution, and that Congress is aware of its limited powers, in such matters, it is the appellant's opinion that the legislative body in enacting Paragraph 5 meant exactly what it said, i.e., that it was unlawful for any person, being an employee of a carrier, riding in or upon any railroad car, motor-truck, etc., of such carrier *transporting passengers or property in interstate or foreign commerce*, to embezzle funds in his custody arising out of or accruing from such transportation. (Emphasis supplied.) Any reasonable interpretation of this language makes it apparent that the word "transporting" governs the words "railroad car, motor truck," etc., and not the words "passengers or property." In order to accept the Government's theory of the case, it is necessary to distort the language of the section until it reads

as follows: "it is unlawful for any person, being an employee of a carrier, riding in or upon any railroad car, motortruck, etc., of such carrier, transporting passengers or property which are moving as or are a part of an interstate or foreign shipment."

It is our opinion that Congress did not so intend, and thus to make it a federal offense for a, as in this case, driver of a local truck to embezzle funds arising from goods which were part of an interstate shipment which were commingled on his truck with local and intrastate freight.

As to the intention of Congress, the Report of the House Committee on the Judiciary is persuasive. Prior to the redrafting of the Section and the addition of Paragraph 5, the Section covered four general situations:

(a) Whoever shall unlawfully break the seal of any railroad car containing interstate or foreign shipments of freight or shall enter such car with intent to commit larceny therein;

(b) Whoever shall steal, etc., from any railroad car (or other specified place) goods moving as or which are a part of or which constitute an interstate shipment of freight, or shall receive the same;

(c) Whoever shall steal, etc., any baggage which shall have come into the possession of any common carrier for transportation in interstate commerce or shall steal the contents thereof or shall receive the same;

(d) Whoever shall steal or shall unlawfully take by any fraudulent device, scheme or game, from any railroad car or from any passenger thereon, when such car is a part of a train moving in interstate commerce any money, baggage, goods or chattels or shall receive the same;

An analysis of the Section as it stood prior to its redrafting indicates that in (a), (b) and (c) the test of jurisdiction is the character of the goods and not the status of the carrier; the only departure from this rule is in (d) where it is clearly stated that the test of jurisdiction shall be "*when such car is a part of a train moving in interstate commerce.*"

In recasting the Section which included the addition of Paragraph 5, the Committee reported as follows:

"The purpose of this legislation is to broaden the scope of the present Larceny Act. The existing statute applies only to larceny of interstate or foreign shipments made by rail, highway or water. *The pending bill combines the crime of embezzlement with that of larceny* and makes the entire act applicable to air transportation. The penalty remains the same as in the present law." (H.R. No. 116, Oct. 10, 1945, U. S. Code Congressional Service 1946, 2-237 Adv. Sheets No. 6; emphasis supplied.)

We respectfully submit that although Congress added the crime of embezzlement to the Section it did not intend to change the test of jurisdiction in this one instance but rather, that the test should remain

the same, that is, embezzlement of property moving as or which are a part of or which constitute an interstate shipment of freight or, under (d) infra, embezzlement from a railroad car or a passenger while on a railroad car, when such car is a part of a train moving in interstate commerce.

We respectfully submit that had Congress intended to radically change the statute in this one particular and, in effect, to confer the status of an interstate carrier upon a local truck merely because it carries, along with other property, goods which are part of an interstate shipment, the Report of the Committee would have so stated.

While it is not controlling, it is equally persuasive that the possible ambiguity present in Paragraph 5 has been clarified by the new Title 18 of the U. S. Code which became effective on September 1, 1948. In the new Code Section 409 has been redrafted into two sections, i.e., Sections 659 and 660. Section 659 covers all of the matter formerly contained in Section 409, Paragraphs 1 to 4 inclusive. Paragraph 5, with which we are concerned, is now covered by Section 660. The language in the pertinent portions of Section 660 are the same with one notable exception: the language in Section 409, Paragraph 5, "vehicle of such carrier transporting passengers or property in interstate or foreign commerce," has been changed, in Section 660, to "vehicle of such carrier moving in interstate commerce." We respectfully submit that if an ambiguity can be spelled out of the language

“transporting passengers or property in interstate or foreign commerce” as used in Section 409, it has been effectively removed from Section 660 by the use of the word “moving.” Of course, inasmuch as the indictment in this case was brought under Section 409 the language in the new Code does not control. It is, however, persuasive in showing the true intent of Congress when both Acts were passed.

It is to be noted also that at the time this indictment was returned Section 412 of the U. S. Code was also in effect. This section reads in part as follows:

“Every president, director, officer or manager of any firm, association or corporation engaged in commerce as a common carrier who embezzles, steals, * * * any of the moneys, funds * * * of such firm * * * arising or accruing from, or used in such commerce * * * shall be deemed guilty of a felony.”

By reading the two sections together we come to one inevitable conclusion. Congress intended that an *officer* of a common carrier could be guilty of the crime of embezzlement wherever funds of the carrier were embezzled, while a mere *employee* of a carrier could be guilty of embezzlement only if he embezzled funds of the carrier while riding upon a vehicle of the carrier which was itself moving in interstate commerce. Congress undoubtedly believed that an embezzlement, such as in this case, by local employee of a carrier, operating a purely local truck could be more effectively prosecuted by the States.

If Congress had wished to achieve the result contended for by the Government it would have more properly and logically amended Section 412 by adding the word employee to the list of persons who could be guilty of the crime of embezzlement of the carrier's funds, wherever the embezzlement occurred.

Finally, if we adopt the interpretation of Section 409 argued for by the Government, it is obvious that the evidence in this case is insufficient to support the verdict. According to the Government, the lower Court had jurisdiction of this offense, and the evidence was sufficient to support the judgment, not because the *vehicle* was moving in interstate commerce but because it was transporting *property* which was in interstate commerce.

A search of the record fails to disclose a scintilla of evidence that, on the dates charged in the indictment, there was any "property in interstate commerce" upon the vehicle *other than the package which, on each occasion the appellant delivered*. It was established also that, on each occasion, the package was delivered, the funds collected and allegedly embezzled. When the package was delivered it ceased to be a part of an interstate shipment. Therefore, there is a total failure of proof, essential under the Government's theory of the case, *that at the time of the alleged embezzlement or at any time thereafter* the defendant was riding upon a vehicle of a carrier, "transporting passengers or property in interstate or foreign commerce."

CONCLUSION.

For the reasons stated, we respectfully submit that the judgment and sentence appealed from should be set aside.

Dated, San Francisco, California,
December 1, 1948.

Respectfully submitted,
JAMES T. DAVIS,
Attorney for Appellant.



No. 11,974

IN THE

United States Court of Appeals
For the Ninth Circuit

WALLACE RAYMOND SHAVER,

Appellant,

VS.

UNITED STATES OF AMERICA,

Appellee.

BRIEF FOR APPELLEE.

FRANK J. HENNESSY,

United States Attorney,

DANIEL C. DEASY,

Assistant United States Attorney,

Post Office Building, San Francisco 1, California,

Attorneys for Appellee.

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No. 11,974

IN THE
United States Court of Appeals
For the Ninth Circuit

WALLACE RAYMOND SHAVER,	}
vs.	
UNITED STATES OF AMERICA,	
	<i>Appellant,</i>
	<i>Appellee.</i>

BRIEF FOR APPELLEE.

JURISDICTIONAL STATEMENT.

The appellee joins in the statements made in appellant's opening brief as to the jurisdiction of the District Court of the United States for the Northern District of California, Southern Division, to try this case, and the jurisdiction of this Honorable Court to consider the pending appeal from the District Court's judgment of conviction. (Appellant's Opening Brief, pp. 1 and 2.)

STATEMENT OF FACTS.

The facts in this case are undisputed. The appellant was employed as a truck driver by the Railway Ex-

press Agency, a carrier of freight and express, on the dates named in the respective counts of the indictment. (Tr. 27.) He drove a truck belonging to the Railway Express Agency in and about San Francisco; he did not drive the truck out of the State of California. (Tr. 28.) In the course of his duties he transported local, intrastate and interstate freight, making deliveries from the railroad yards to the consignees. (Tr. 28.)

On each of the two occasions mentioned in the indictment, the appellant delivered an interstate shipment of freight to the consignee and collected charges arising out of and accruing from the transportation of the freight in interstate commerce, including taxes, express charges, value charges, C.O.D. charges and C.O.D. service charges. (Tr. 30.) He embezzled these funds and converted them to his own use. (Tr. 34-35.)

ARGUMENT.

The indictment in this case is the first to be returned in this District charging a violation of U.S. Code, Title 18, §409, as amended in 1946 (60 Stats. 656).

Prior to that amendment §409 made it a criminal offense to:

1. Break the seal of a railroad car containing interstate shipments of freight or express with intent to commit larceny.

2. Enter such a car with like intent.

3. Steal, take, carry away or conceal, or by fraud or deception obtain with intent to convert to one's own use, from certain specified places, any goods moving as or which are a part of or which constitute an interstate shipment of freight or express.

4. Buy, receive or have in one's possession any such goods, knowing them to have been stolen.

5. Steal, take, carry away, or by fraud or deception obtain with intent to convert to one's own use any baggage which shall have come into the possession of any common carrier for transportation in interstate commerce.

6. Break into, steal, take, carry away, or conceal any of the contents of such baggage.

7. Buy, receive or have in one's possession any such baggage or contents, with knowledge that it was stolen.

These categories may be summarized by stating that they penalize the burglary of a railroad car, the larceny of goods moving as or comprising a part of an interstate shipment, larceny of baggage or the contents of baggage entrusted to a carrier for interstate shipment, and receiving property stolen in violation of this section.

“The essential object of this statute is to create, define, and punish the offense of abstracting or unlawfully having in possession goods

while in interstate or foreign transit, and thereby interfering with interstate or foreign commerce.”

White v. U.S., 273 Fed. 517.

By amendment in 1946, Title 18 U.S. Code § 409 was revised and expanded in several respects.

1. It was reworded to make it applicable to burglary of vessels, aircraft, wagons and motor trucks, as well as railroad cars.

2. It included embezzlement of goods moving as or which are a part of or which constitute an interstate shipment of freight or express, and added aircraft and air navigation facilities to the places from which larceny or embezzlement is prohibited.

3. It included embezzlement of baggage or contents of baggage entrusted to a carrier for interstate transportation.

4. It made it a criminal offense to “embezzle, steal, or unlawfully take by any fraudulent device, scheme, or game from any railroad car, motor truck, steamboat, vessel, aircraft, or other vehicle operated by any carrier, or from any passenger or employee thereon, when such railroad car, or the train of which it is a part, motor truck, steamboat, vessel, aircraft, or other vehicle is moving in interstate or foreign commerce any money, baggage, goods or property” with intent to convert the same to one’s own use, or to buy, receive or have in one’s possession any such money,

baggage, goods or property, knowing the same to have been embezzled or stolen.

5. It made it a criminal offense for anyone who shall "being an employee of any carrier riding in, on or upon any railroad car, motor truck, steamboat, vessel, aircraft or other vehicle of such carrier transporting passengers or property in interstate or foreign commerce and having in his custody funds arising out of or accruing from such transportation, embezzle or unlawfully convert to his own use any such funds."

It will readily be seen that in addition to enlarging the scope of the several categories of offenses denounced by the old statute, the amendment set up two entirely different classes of offenses, Federal jurisdiction over which is dependent upon totally different aspects of interstate commerce.

In the old statute, the property involved in the larceny or receiving was only such property as constituted an interstate shipment, or which was actually moving in interstate commerce.

The amended statute (Subsection (4)) makes it an offense against the United States for anyone to commit a larceny or embezzlement of *any property upon* a vehicle when that vehicle is moving in interstate or foreign commerce. The test here is not whether the *property* is part of or constitutes an interstate or foreign shipment. The test is whether the *vehicle* is moving in interstate or foreign com-

merce. Larceny upon a transcontinental train or airplane is made a Federal offense, somewhat akin to larceny upon the high seas, or upon lands within the exclusive jurisdiction of the United States. This paragraph of the amended statute applies to larceny or embezzlement of money or property which is *not* moving in interstate or foreign commerce, but which is stolen or embezzled from a vehicle which *is so moving*. It would apply, for example, to the theft of property belonging to a passenger traveling from San Francisco to Truckee, California, on a train en route from San Francisco, California to Ogden, Utah.

Subsection 5 of the amended statute, under which the indictment in this case is laid, makes it an offense to embezzle funds accruing from the interstate transportation of freight or express. The embezzlements punishable under this paragraph of Section 409 are by the terms of the statute only embezzlements committed by employees of a carrier riding upon vehicles of their employer, which vehicles are transporting passengers or property "in interstate or foreign commerce".

In his brief appellant argues that this means embezzlements of funds accruing from the interstate transportation of property which has been carried *on the vehicle* upon which the employee is riding, FROM ONE STATE TO ANOTHER.

We do not believe any such interpretation to be the intention of Congress, nor do we feel that it is a proper construction of the language of the statute.

Had Congress intended to penalize only such embezzlements, there would have been no necessity to enact this portion of the statute at all, since such embezzlements are included within the language of subdivision (4) "embezzle * * * or unlawfully take * * * from any * * * motor truck when such * * * motor truck is moving in interstate or foreign commerce, any money * * * with intent to convert the same or any part thereof to his own use".

We believe that subsection 5 of § 409 is intended to and does by its very terms penalize embezzlements by a carrier's transit employees (as opposed to office employees) who ride upon the carrier's vehicles, making deliveries of property which is or constitutes a part of an interstate shipment of freight or express.

A vehicle which makes the initial or the terminal haul is as much engaged in transporting property in interstate commerce as the vehicle which carries the property across the line from one State to another.

The shipments delivered by appellant in this case were "door to door" shipments. (Tr. 21.) From the time they left the possession of the consignor until they were delivered by appellant to the consignees they were being transported in interstate commerce. While making those deliveries and collecting the charges accruing from the interstate shipment of the goods so delivered, appellant was riding upon a vehicle of the carrier "transporting property in interstate commerce".

Property is in interstate commerce from the time it leaves the hands of the consignor until it reaches the hands of the consignee.

Boyd v. U.S. (CCA-4), 275 Fed. 16;

Friedman v. U.S. (CCA-1), 233 Fed. 429;

Sharp v. U.S. (CCA-5), 280 Fed. 86.

Argument is made in appellant's brief that if the statute means what appellee contends it does mean, then we must conclude that the jurisdiction of the United States to regulate commerce between the States extends to regulation of every vehicle upon which a package constituting a part of an interstate shipment might be carried. We do not believe any such conclusion follows from our argument in this case.

Appellant concedes that the shipments delivered by him comprised interstate shipments until delivered to the consignees. It is likewise undisputed that the funds embezzled by appellant accrued from interstate transportation of the property; but the argument is advanced that at the moment the embezzlement in each instance took place, there was no interstate shipment remaining undelivered on the appellant's truck, and therefore he could not have been riding upon a truck transporting property in interstate commerce, and therefore the embezzlements are not covered by the statute.

We think this argument is without merit. From a reading of the amended statute in its entirety it seems

obvious that in enacting Subdivision 5, Congress intended to penalize exactly the thing which was done by appellant in this case, namely, the embezzlement of funds accruing from interstate transportation of property by the employees of carriers who have collected the funds after making delivery of the property. In the ordinary course of events, the charges would not accrue until the transportation had been completed, and the funds would not be collected until the delivery had been made.

The regulation of interstate commerce is within the power of Congress; and this has been held to include the power to fix rates and charges for transportation of property. In like manner, Congress has power to provide penalties for interference with interstate commerce, including such activities as larceny and embezzlement of property moving in interstate commerce or comprising interstate shipments of freight or express. It seems to us that Congress may also make it a criminal offense for employees of carriers engaged in interstate commerce to embezzle the funds accruing from interstate shipments and that the statute involved in this case was intended to and does have that effect, and that the argument that the vehicle must proceed across a State line, or that at the time of the embezzlement there must remain on the vehicle another undelivered interstate shipment is without merit.

CONCLUSION.

For the reasons stated we respectfully submit that the judgment of the District Court should be affirmed.

Dated, San Francisco, California,
January 7, 1949.

Respectfully submitted,

FRANK J. HENNESSY,

United States Attorney,

DANIEL C. DEASY,

Assistant United States Attorney,

Attorneys for Appellee.

No. 11975 and No. 12012

IN THE

**United States
Circuit Court of Appeals**

FOR THE NINTH CIRCUIT

F. E. NEMEC, *Appellant,*
vs.

UNITED STATES OF AMERICA,
Appellee.

} No. 11975

BONEWICZ X. DAWSON, *Appellant,*
vs.

UNITED STATES OF AMERICA,
Appellee.

} No. 12012

On Appeal from the District Court of the United
States, for the Eastern District of Washington

BRIEF FOR THE APPELLEE

HARVEY ERICKSON,
United States Attorney

FRANK R. FREEMAN,
Assistant United States Attorney,

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No. 11975 and No. 12012

IN THE

United States
Circuit Court of Appeals
FOR THE NINTH CIRCUIT

F. E. NEMEC, <i>Appellant</i> , <i>vs.</i> UNITED STATES OF AMERICA, <i>Appellee.</i>	}	No. 11975
BONEWICZ X. DAWSON, <i>Appellant</i> , <i>vs.</i> UNITED STATES OF AMERICA, <i>Appellee.</i>	}	No. 12012

On Appeal from the District Court of the United
States, for the Eastern District of Washington

BRIEF FOR THE APPELLEE

STATEMENT OF JURISDICTION

The Circuit Court of Appeals has jurisdiction of the instant case under the provisions of Title 28, Sec. 1291, USCA, and the prosecution in the lower court was based upon Title 18, Secs. 338 and 88, and Title 15, Sec. 77(q).

STATEMENT OF THE CASE

On the 5th day of May, 1948, a United States Grand Jury sitting at Spokane, Washington, returned

an indictment against appellants F. E. NEMEC, BONEWICZ X. DAWSON and others. This indictment in substance charged as follows:

“Count I.

That between January 1, 1945 and continuing to the date of indictment, the defendants, F. E. NEMEC, BONEWICZ X. DAWSON, STANLEY E. RICHARDSON, DR. HAROLD R. RECTOR, WESTCOTT B. CLARKE, FLORA L. CARPENTER, and H. P. SCHWARTZ, conspired, combined, confederated and agreed with each other and with divers other persons whose identity is to the grand jurors unknown * * * * to violate Title 18, Sec. 338, U.S.C.A., by devising * * * * a scheme and artifice to defraud investors and for obtaining money and property from investors in investment contracts and certificates of interest or participation in profit sharing agreements relating to placer and lode gold mining claims and operations in Sierra and Butte Counties, California, and ore processing operations at Crescent City and Los Angeles, California * * * * to be executed through * * * * the United States mails by means of false and fraudulent pretenses, representations and promises, the defendants well knowing at the time that said pretenses, representations, and promises would be false when made; and,

Violations of Title 15, Sec. 77(q), U.S.C.A., by using * * * the United States mails to employ said scheme and artifice to defraud said investors * * * *.

That said false and fraudulent pretenses, representations and promises included, among others, the following:

1. That said defendants, doing business as Northwest Mining and Engineering Company, a partnership, would and did locate valid, patent-

able, placer mining claims for investors on Government land, open for the location of mineral placer claims, in Sierra County, California, which claims were highly valuable.

2. That under state and federal laws relating to the location of mining claims, no individual or corporation could locate more than one 20-acre placer gold mining claim.

3. That hydraulic placer mining operations on the Sierra County sites had been prevented and rendered illegal by statute and injunction from 1886 until immediately prior to World War II.

4. That the placer mining claims located and to be located for investors had valuable standing timber which could and would be removed and sold by Northwest Mining & Engineering Company, the proceeds of which would inure to the benefit of the claim holders in an amount sufficient to repay the total original investments for their claims.

5. That the placer claims which defendants would and did locate for investors in Sierra County, California, contained values in gold of 40 cents per cubic yard, or over, and would produce net monthly returns to investors of \$30.00 for each claim located.

6. That the defendants, doing business as Northwest Mining & Engineering Company, had acquired all necessary water rights, water conduit ditches, and rights of way necessary to enable them to efficiently hydraulic the claims which they would and did locate for investors in Sierra County.

7. That defendants and Northwest Mining & Engineering Company had adequate and ample finances with which to set up and carry on a large scale placer mining operation on claims which they would and did locate for investors.

8. That defendants had arranged for the purchase and operation of the Sierra Butte Mine, the earnings from which would inure to the benefit of all investors for whom defendants located placer mining claims.

9. That the defendants through Northwest Mining & Engineering Company, had discovered in the immediate vicinity of their placer mining operations in Sierra County, California, a vein disclosing valuable gold lode or quartz deposits.

10. That the defendants, through Northwest Mining & Engineering Company, would and did locate for investors valid, legal, lode mining claims consisting of eight such 20-acre lode claims on government land, open for location of lode mining claims, in Sierra County, California.

11. That the lode claims located and to be located in Sierra County, California, by defendants for investors had valuable standing timber which could and would be removed and sold by Northwest Mining & Engineering Company, the proceeds from which would inure to the benefit of the claimholders in an amount sufficient to repay the total original investments for their claims.

12. That based upon successful placer mining operations of the Northwest Mining & Engineering Company at Sierra City, California, an early distribution of substantial earnings had been and would be made to investors in lode claims.

13. That the defendants, doing business as Northwest Mining & Engineering Company, would and did locate valid, patentable, placer mining claims for investors on government land, open for location of mineral placer claims, along and adjacent to the ancient Mammouth, Magelia and Nimsheew channels in Butte County, California.

14. That defendants could and would operate all said placer mining claims located for investors in Butte County, California, in a single unified underground placer mining operation.

15. That the defendants, through Northwest Mining & Engineering Company, had acquired all necessary mining and tunnel rights to a property in Butte County, California, commonly referred to as the California Treasure Box, Ltd., through which a unified underground placer mining operation on claims located for investors could and would be carried on.

16. That the defendants, through Northwest Mining & Engineering Company, would and did thoroughly and adequately sample and test for gold values the claims in Butte County, California, which they would and did locate for investors.

17. That the defendants, through Northwest Mining & Engineering Company, had performed all necessary preliminary engineering work to permit immediate commencement of underground placer mining operations on claims in Butte County, California, which they would and did locate for investors.

18. That Northwest Mining & Engineering Company had retained the services of Dr. Harold R. Rector, chemist, nuclear physicist, eminent chemical engineer, and key atomic scientist in the development of the atomic bomb at the Hanford Project.

19. That said defendants, doing business as Northwest Mining & Engineering Company and Crescent City Mining Company, had obtained exclusive rights to a secret process invented by Dr. Harold R. Rector by means of which a commercial and highly profitable recovery of gold and other metals could be made from the black

sands and other ores in the vicinity of Crescent City, California.”

This count further set forth fifteen overt acts allegedly committed by the defendants in pursuance of said conspiracy and to effect its objective.

“COUNT II.

1. That prior to January 1, 1945, and continuing to November 6, 1947, the defendants, F. E. NEMEC and BONEWICZ X. DAWSON, devised * * * a scheme * * * * to defraud investors * * * * in investment contracts and profit sharing agreements relating to the location and operation of placer and lode gold mining claims in Sierra and Butte Counties, California, and to ore processing operations at Crescent City and Los Angeles, California, by means of fraudulent pretenses, representations and promises, including among others those mentioned in Count I of this indictment and numbered from “1” to “19”, inclusive* * * knowing that said pretenses, representations and promises would be false when made.

2. That on the 13th day of December, 1945, * * * * the defendants, F. E. NEMEC and BONEWICZ X. DAWSON, for the purpose of executing the aforesaid scheme * * * * caused to be sent and delivered * * * * by the post office establishment of the United States, a letter addressed to Mr. Henry L. Harris, 921 Snow, Richland, Washington.”

“COUNT III”

Count III was dismissed on motion of the United States Attorney prior to the trial.

“COUNT IV.

1. That the defendants F. E. NEMEC and BONEWICZ X. DAWSON, so having devised the scheme and artifice to defraud described in Count I of this Indictment * * * * did in the sale of a security, to-wit: investment contracts and profit sharing agreements relating to location and operation of placer and lode gold mining claims in Sierra and Butte Counties, California, and ore processing operations at Crescent City and Los Angeles, California, by use of the United States mails, employ the said scheme * * * * in the manner following, to-wit:

2. The said defendants on or about the 9th day of November, 1946, * * * * did cause to be delivered by the mails of the United States * * * * a certain letter addressed to Robert L. and Catherine U. Alderson, Route No. 8, Yakima, Washington, the said letter having * * * * on or about the 8th day of November, 1946, been placed * * * * by said defendants in an authorized depository for mail matter to be sent or delivered by the post office establishment of the United States according to the directions thereon.”

in violation of Title 15, Sec. 77 (q) (a) (1) USCA, also known as Sec. 17 (a) (1) of the Securities Act of 1933, as amended.

“COUNT V.

1. The grand jury realleges all of the allegations of Count IV of this Indictment except those contained in the second paragraph thereof.

2. The said defendants on or about February, 1946 * * * * did cause to be delivered by the mails of the United States * * * * a certain mimeographed sales brochure addressed to G. E. Hall, 1425 Kimball, Richland, Washington; the said sales brochure having theretofore been

placed or caused to be placed by the said defendants in an authorized depository for mail matter in Seattle, Washington, to be sent or delivered by the post office establishment of the United States according to the directions thereon."

in violation of Title 15, Sec. 77 (q) USCA, also known as Sec. 17 (a) (1) of the Securities Act of 1933, as amended.

The various counts of the indictment in substance charged that appellants Nemec and Dawson devised a scheme to defraud investors and to obtain money and property from investors by false and fraudulent pretenses, representations and promises. The scheme was a continuing one covering a period from approximately January 1, 1945 to the date of the indictment. In carrying out the scheme, the appellants formed various partnerships and carried out numerous successive promotions from which approximately \$180,000 of investors' funds were obtained.

In the first phase of the scheme, appellant Nemec, who will hereinafter be referred to as "Nemec", obtained from appellant Dawson, hereinafter referred to as "Dawson", information relating to certain mining property in the vicinity of Sierra City, Sierra County, California. (Tr. 1373) In early 1945 Nemec formed a Washington partnership with his wife under the name of the Northwest Mining and Engineering Company, hereinafter referred to as "Company", with offices in Seattle, Washington. By personal contacts, as well as by sales brochures and through salesmen, Nemec represented to investors that the Com-

pany had obtained control of a valuable placer property at Sierra City, California and had determined that extensive areas of Government land in the vicinity of this property was open for location of placer mining claims. Investors were solicited to employ the company to locate 20-acre placer mining claims in this area, for a "fee" of \$280 each, to be grouped together into 160-acre "association" placer claims, and were assured that when a large area of such claims had been blocked up, the claims would be leased by the Company who would then engage in a large scale hydraulic mining operation on the property which it controlled and on which claims had been located. Claim holders would be paid on a pro-rata basis from the funds set aside from the smelter returns. It was represented that the claims were being offered to Washington residents in order that local California people might not become aware of the Company's plan which possibly might precipitate a gold rush.

Shortly after the sale of placer claims was under way, it was claimed that valuable lode veins had been located in the area and many of the old, as well as the new, investors were induced to become lode claim holders for a fee of \$480 per claim. Lode claim holders were to participate both in the returns from the placer operations and in the lode operations.

Coincident with the sale of placer and lode claims at Sierra City, Nemec organized the Sierra City Mining Company, a limited partnership, purportedly to carry on the operations at Sierra City. These

partnership interests were offered at the rate of \$1200 for a 1% interest in the earnings after payment of expenses. Partners were promised repayment of their investment from the first earnings of the operation. Although this was to be the working and operating company of the Sierra City enterprise, the books of account of Northwest Mining and Engineering Company disclosed no transfer of assets to the Sierra City Mining Company.

In all, approximately \$85,000 was obtained from investors in Sierra City placer and lode claims and partnership interests in the Sierra City Mining Company. (Tr. 1589) While Nemec was active in the raising of funds, Dawson received an expense account and in accordance with his agreement with Nemec, was to share in the ultimate profits. (Tr. 1420)

The majority of the placer and lode claims were actually located upon lands already owned by others under patents or upon land withdrawn from entry and location and it was shown that Nemec had been so advised by both the County Engineer, Taylor, and the Forest Ranger, Delaney. The lode claims were so improperly described that they could not be located or platted. (Tr. 64)

While the Sierra City operations were still being carried on with false pretenses of early dividends, Nemec and Dawson commenced examining additional property in Butte County, California upon which a similar plan of locating placer claims might be followed. Dawson admitted calling this to Nemec's atten-

tion. (Tr. 1423) A campaign was then commenced for the sale of placer mining claims at a "fee" of \$385. per 20-acre claim in the area commonly referred to as the Mammoth Channel in Butte County, California. This Mammoth Channel was an ancient river channel covered by a deep lava overcapping. In the sales brochure prepared by Nemec, (Pl. Ex. 55, p. 2176) it was represented that forty 160-acre association placer claims could be located in the area of this channel and operated as a single unit using a plan of underground sluicing through a tunnel under the ancient river channel commencing at a place where Big Butte Creek had cut through the lava overcapping to expose the ancient channel. Maps in cross-section and geographic detail (Pl. Ex. 5) were used by Nemec to present the plan to investors. The tunnel site, necessary for the mining operation as portrayed by Nemec, was claimed to have been acquired by the Company and located on property known as the California Treasure Box, or on property of the Pacific Gas and Electric Company. This fact was denied by the owners of these properties. As shown by the official records and depicted on the map prepared therefrom (Pl. Ex 6), no other land in the area where Big Butte Creek intersects the Mammoth Channel was open for the location of mining claims or for tunnel site purposes. Claims were to be located in a continuous area over the course of the Mammoth Channel as shown on the map exhibited to investors by Nemec.

As in the case of Sierra City claims, many of the Mammoth Channel claims were located upon patented

land and on lands not open to mineral entry because of withdrawal for power site purposes or prior locations. The claims as located were scattered over a thirteen mile area making impossible a continuous unified operation as represented by Nemec. (Pl. Ex. 6, Tr. 104-106) When it became apparent to Nemec and Dawson that claim holders had learned of the invalidity of the claims located for them in this area, Dawson relocated nearly all the claims. Even the relocations, however, were widely scattered and not susceptible to a unified operation and were again chiefly located on power withdrawn lands. (Pl. Ex. 6, Tr. 103-104)

Approximately \$40,000 was obtained from investors in the Mammoth Channel promotion and no mining operations of any kind were ever commenced although investors were assured from time to time that operations were about to commence. It is apparent from the invalidity of the claims themselves in addition to their being scattered over a thirteen mile area, that no mining operation could be commenced in this area.

While the sale of claims in Mammoth Channel was still under way, representations were being made by Nemec to investors and prospective investors that an eminent atomic scientist of the Hanford Atomic Energy project, Dr. Harold R. Rector, had become associated with the Company. (Tr. 636) It was represented that Dr. Rector was to head a project for the recovery of gold from black sands at Crescent City by the use of an atomic process which he had

developed. Dawson, Nemec and Rector assisted in obtaining newspaper publicity relating to Rector's achievements and reprints of this article were circulated by Nemec to investors. (Tr. 819) Nemec also had Rector give lectures on the atomic theory to prospective investors coming to Crescent City. (Tr. 960-966) To provide a vehicle for this phase of the scheme, a new partnership was formed known as the Crescent City Mining Company in which interests were offered to investors at the rate of \$1200 for a 1% interest, and approximately \$60,000 was raised by the sale of these interests. No returns of any kind were paid to investors.

The Government presented substantial evidence that the nineteen specific misrepresentations set forth in the indictment were made to investors by Nemec either in person, through sales literature or through salesmen instructed by Nemec. Substantial evidence was presented proving the falsity of these misrepresentations. Since it would unduly extend this statement to detail the evidence introduced by the Government relating to all of the nineteen misrepresentations, only the most important of those misrepresentations and the evidence refuting same will be referred to.

The essence of the plan by which investors were induced to enter contracts for Sierra City placer claims, Sierra City lode claims, and Mammoth Channel placer claims was the representation that lands in each of these areas were open for the location of the claims. (Tr. 246, 2154, 2176) It was represented that the claims could be patented if desired by the claim holder. (Tr. 143, 180) Ross F. Taylor, a civil

engineer and former County Assessor, testified in refutation of the above report that from his examination of the Sierra County records and Government records, only five of the approximately fifteen association placer claims at Sierra City were not located fully or partially upon patented, previously located land or on power withdrawn areas not open for location. (Tr. 73-78) Similar testimony by Taylor was given relating to lode claims.

In the case of the Mammoth Channel claims in Butte County, the testimony of Martin L. Polk, civil engineer and County Assessor, disclosed that the majority of the thirteen original association claims were located either on land already patented or withdrawn for power site purposes and therefore invalid. Mr. Polk further testified that of the ten relocations of said association placer claims made by Nemec and Dawson, these relocations were almost entirely upon lands withdrawn from mineral entry or for power withdrawal purposes and therefore again invalid. (Tr. 98-106)

As a background for the original offering of mining claims in the vicinity of Sierra City and as explanation for the reason that investors were being solicited to locate placer claims, it was represented by Nemec that no person could file on more than one 20-acre placer claim (Tr. 177-178) and for this reason it was necessary to obtain a large number of investors in order to block up a large area for hydraulic operations. The falsity of this representation is apparent. As correctly instructed by the Court,

no such limitation exists in law, the only limitation being that no person may hold more than one 20-acre placer claim in an association of eight claims.

Sierra City lode and placer claim investors were assured by Nemec that regardless of the outcome of the mining operations, their investments were risk free because sufficient profits could be obtained from the removal of the timber upon claims to repay the amount of the investment. (Tr. 207-208) In addition to the fact that many of the claims were invalid because located on lands not open for mineral entry and consequently timber therefrom could not legally be removed, the Government further refuted this representation through the testimony of Frank B. Delaney, U. S. Forest Ranger in charge of the Sierra City area. Mr. Delaney testified that he was thoroughly acquainted with the claims at Sierra City and the timber thereon and that there was no merchantable timber on any of the claims. (Tr. 409-421.) It was further represented to investors of the Sierra City operation that an option on the Sierra Butte mine had been obtained by Nemec and Dawson on behalf of the Company and that earnings from its operation would inure to the benefit of claim holders. (Tr. 147, 181, 209.) Clarke, one of Neme's salesmen and a defendant in the conspiracy, admitted when impeached by previous testimony given under oath before a Government investigator, that he had made such representations and that Nemec had furnished him the information. (Tr. 1257-1258) To prove the

falsity of such representations, the Government produced as its witness one Elistus L. Hayes whose family has owned the Sierra Butte mine for the past forty years and who testified that although approached by Dawson with reference to an option and a lease on that property, he unequivocally refused then or at any subsequent time to give Dawson or Nemec or the Company any lease, option or right to purchase or operate the mine. (Tr. 451)

It was represented to investors that the claims located along Mammoth Channel in Butte County, California would be operated in a single unified underground placer mining operation and it was further represented that approximately 5400 acres of land had been determined to be available for the location of claims in this area. (Tr. 567-568) The advantages of working the large block of claims in a unified operation were dealt with in considerable detail. As has already been pointed out hereinbefore in our Statement of the Case, the falsity of this representation is apparent from plaintiff's exhibit "6" which shows all of the association placer claims actually placed by Nemec and Dawson on the Mammoth Channel to be scattered over a thirteen mile area making a single unified operation impossible.

It was further represented that a tunnel site in the area of Mammoth Channel had been acquired at the intersection of Big Butte Creek with the claimed course of the Mammoth Channel and this tunnel site was pointed out to investors on the sales map of the Mammoth Channel area used by Nemec and

his salesmen. (Pl. Ex. 79) In this connection some investors were told that the tunnel site was on property known as the California Treasure Box and the Company had control of that property. (Tr. 488) Other investors were told that the tunnel site was on the property of the Pacific Gas and Electric Company and that a lease had been secured with the Pacific Gas and Electric Company for tunnel rights on said property. (Tr. 321, 534-535) To prove the falsity of these representations, the Government called as its witness one Marcel Schmidt who testified that he has been the owner of the California Treasure Box since February of 1945 and that at no time did he execute a lease or option of the tunnel site on said property or any purchase of said property to either of the appellants here or to the Northwest Mining and Engineering Company. (Tr. 807-808) Mr. Cullen W. Coates, a representative of the Pacific Gas and Electric Company and called by the Government as its witness, testified unequivocally that his company had made no lease or given any commitment on its property in the Mammoth Channel area to either of the appellants here or to the Northwest Mining and Engineering Company. (Tr. 692-695) The crux of operations in Mammoth Channel, as explained by Nemec to investors, was based upon possession of a tunnel site at Big Butte Creek. Without the possession of that site the operation outlined by Nemec was impossible.

It was represented to investors and prospective investors that Nemec and the Company had obtained the services of an eminent nuclear physicist, Dr.

Harold R. Rector, and that Dr. Rector had demonstrated a secret process by which gold could be obtained from black sands through the use of atomic processes. (Pl. Ex. 149, Tr. 636) The Rector process was to be used in operations at Crescent City. In proof of the falsity of this misrepresentation, Dr. Rector himself took the stand and admitted that he had no background as an atomic scientist or nuclear physicist but that rather, he was a chiropractor employed at the Hanford Atomic project as a water tester. (Tr. 838-839) Rector further testified that he disclosed his lack of qualifications to Nemec and to Dawson and that the latter commented about his being a chiropractor. (Tr. 877) Rector also under Nemec's direction, gave so-called "fireside chats" to prospective investors coming to Crescent City on his atomic process for gold recovery with the sole purpose of impressing investors and prospective investors. (Tr. 876, 960-966)

APPELLANT NEMEC'S ASSIGNMENTS OF ERROR

The appellant Nemec's assignments of error will be discussed in the order in which they are set forth in the appellant's brief.

ARGUMENT

1. Answer to Appellant Nemec's Assignment of Error No. 1, viz., That The Verdict, Insofar as the Appellant Nemec is Concerned, is Contrary to Law. The Evidence is Insufficient to Support the Conviction.

The Appellant Nemec was the President of the Northwest Mining and Engineering Company and

was the principal defendant in the case. Counsel for appellant Nemec stated that the jury was permitted to find a verdict of guilty without the necessary careful discriminating assessment of the guilt of the defendants. The statement is in error as appellant Nemec's counsel at the time of trial were satisfied with the instructions and failed to except thereto. (Tr. 1944) This appellant cites the case of *Kotteakos v. United States*, 328 U. S. 750 as authority for the claim that this case was tried upon wrong theory. In the Kotteakos case there were several conspiracies consisting of independent groups unknown to the other, and in this case there was one closely knit group all working together for one common object, to-wit: the swindling of the public by sale of mining claims, mining leases, partnerships and interests in atomic processes—anything to take in the money for one common objective, the enrichment of the appellant F. E. Nemec, the chief partner in the Northwest Mining and Engineering Company.

Nineteen different misrepresentations are charged to the appellant Nemec and his co-conspirators. Appellant's counsel now seeks to go over more than a thousand pages of the record with a high powered magnifying glass and point to certain specific instances where he thinks certain of the misrepresentations have fallen by citing some particular answer of a particular witness to a particular question. The whole matter of these alleged misrepresentations was submitted to the jury by careful and appropriate instructions which satisfied the appellant at the time they were given.

The evidence, when considered as a whole, is conclusive as to the fraudulent nature of the misrepresentations. It is submitted that this Court in reviewing the record at this time must take the view of the evidence which is most favorable to the Government and accept as true all the facts which the evidence reasonably tended to prove.

Boushea v. United States, 173 Fed. (2d) 131.

II. *Answer to Appellant Nemec's Assignment of Error No. 2, viz., That the Court Erred in the Admission of Exhibit 211, it Being Highly Prejudicial to the Appellant Nemec on the Theory on Which the Case was being Tried.*

Exhibit 211 is a desist and restraining order restraining the appellant Nemec from selling securities in the State of California. Appellant Nemec testified elaborately as to his employment and life from the year 1907 including the service of a term in the penitentiary for a violation of the Securities Act and subsequent operations in California and Arizona. (Tr. 1486-1500) He carefully omitted the part about a restraining order being entered against him in the State of California. Cross examination as to the California restraining order merely filled in a gap in the picture of a life history which he gave to the jury.

Also, all claims sold to investors were sold to residents of the State of Washington. Appellant Nemec and his salesmen told many of the Washington investors that the reason that these claims were not sold in the State of California where they were located was that if the fact ever became known to

residents in California that the claims were being located there, another California gold rush would be precipitated and the natives in California who were near the scene would have an opportunity of seizing the ground and eliminating outsiders, including the prospective investors in the State of Washington, from being able to get any of the claims. An example of these statements comes out in the testimony of the investor witness Smiley (Tr. 142) and the investor witness Dawes (Tr. 178).

In view of the reason assigned by the appellant for making his claims available to Washington investors—a logical one as far as the investors were concerned as they believed that they were being befriended by the appellant by being permitted to make this investment—the Government in all fairness should be permitted to show another reason why the appellant Nemec was not offering claims in the State of California—because there was a restraining order against him preventing him from so doing.

In view of the evidence it was only equitable and just to submit both these reasons to the jury so that the jury could say which one was more likely to be true—whether or not the appellant was imbued with the philanthropic spirit of aiding Washington investors or whether the California restraining order may have been a motivating force in keeping him from selling his claims in that state.

III. *Answer to Appellant Nemec's Assignment of Error No. 3, viz., That the Court Left a Matter of Law to the Discretion of the Jury in Allow-*

ing Them to Rule as to Whether or Not the Partnership Agreements were Within the Scope of the Securities and Exchange Commission Act.

This assignment of error is argued elsewhere in this brief at page 38 and will not be again argued here.

IV. Answer to Appellant Nemec's Assignment of Error No. 4, viz., That the Court Erred in Instructions Given.

As previously explained, no exceptions were taken by appellant Nemec's counsel at the time the Court instructed the jury as to the erroneousess of any of the instructions. In view of that fact, this Court should not at this time consider error in the instructions unless it is of such greivous nature that the Court of its own volition should notice it. Counsel does not so contend.

V. Answer to Appellant Nemec's Assignment of Error No. 5, viz., That Letters from the Defendants Were Admitted Which Were Entirely Outside the Scope of the Indictment Since They Were Either Written in many Instances Long After the Money had Passed to the Defendants, and thus were not Under any Conceivable Theory Part of the Inducement for which the Money was Passed or were Written After the Finding of the Indictment.

As has previously been argued in this brief, the enterprises of the Northwest Mining and Engineering Company were continuing from early in the year 1945 down to the return of the indictment in May, 1948. The appellant intended to reload the investors in other enterprises so that the fraud was continu-

ing, the thought in view being to reload each investor as many times as possible in order to obtain as much as the traffic would bear.

These letters which counsel refers to would also be admissible as lulling letters as they were used to communicate with the investors and lull them into a sense of security when the Northwest Mining and Engineering Company had no intent or prospects of ever paying out or performing in accordance with those letters.

Brady v. United States, (CCA9) 26 Fed. (2d) 400 Cert. Den. 278 U. S. 621.

Certain letters were admitted after the return of the indictment which were written by the appellant Dawson. These letters were admitted without objection by appellant Dawson's counsel and were admitted under cautionary instruction of the Court to regard them only against Dawson. (Tr. 1458-1459)

VI. Answer to Appellant Nemec's Assignment of Error No. 6, viz., That the Court Erred in Refusing to Permit the Admission of Exhibit 150 (Tr. 801 and 802) Thereby Depriving the Appellant Nemec of the Oportunity to Prove who Wrote the Article of October 11, Concerning the Qualifications of Dr. Rector.

Exhibit 150 referred to a page in the Del Norte Triplicate containing an article written by someone connected with the newspaper condemning the Securities and Exchange Commission for certain practices of inconsiderate dealings with mining promotions and lack of enthusiasm for new methods. (Tr. 824) This was the same paper which published laudi-

tory articles of Dr. Harold R. Rector as an eminent scientist, nuclear physicist, and atomic scientist. No showing of materiality to any of the issues in this case can be made about the newspaper article written by some anonymous author condemning the activities of the Securities and Exchange Commission. Even if the Securities and Exchange Commission was guilty of all the vices and inequities charged, such would not detract from the guilt or innocence of the appellants.

VII. Answer to Appellant Nemec's Assignment of Error No. 7, viz., That a co-defendant was Pleaded Guilty Before the Jury Panel and Then Permitted to Change his Testimony Before the Very Jury Chosen from that Panel. Proper Safeguarding Instructions were not Given by the Lower Court.

The answer to this argument is set forth fully in this brief, page 34, and will not again be discussed here with the exception that it is submitted that the Court did give proper cautionary instructions in his charge to the jury as to the guilt or innocence of Dr. Rector having an effect on the guilt or innocence of other co-defendants. The Court in his charge to the jury adequately protected the other defendants by the following language:

"The fact that the defendant Harold R. Rector, in your presence, pleaded guilty to the charge of conspiracy shall be disregarded by you in determining the innocence or guilt of all the remaining defendants, for under the terms of the indictment the said defendant Rector is charged with having conspired with some person or persons not known or named in the indictment, other

than and as well as the other defendants, and this he may have done without any involvement of the remaining, named defendants." (Tr. 1929)

It is submitted that this instruction protected the remaining defendants as far as it was humanly possible to do so by any instruction. Counsel assigned as error the giving of an instruction that the witness Harold R. Rector is what is known as an accomplice and that such operates against the credibility of his testimony. (Tr. 1935) This instruction was in favor of the appellants because the jury was told that Rector was an accomplice and that his testimony should be scrutinized with great care.

In any event it may be stated that no exceptions were taken to any of these instructions at the time given and as were required by law and rule of this court. Counsel for appellant Nemec complained that Dr. Rector was guilty of perjury and was not indicted but placed upon probation and assessed no fine. Argument made that Dr. Rector is guilty of perjury and was not sufficiently punished is extraneous to any of the issues in this case and will not be discussed.

VIII. Answer to Appellant Nemec's Assignment of Error No. 8, viz., That the Court Erred in Permitting Inflammatory Remarks by the United States Attorney in his Argument to the Jury which Remarks had Nothing to do with the Evidence which had been Adduced at the Trial.

It is now charged for the first time that certain inflammatory statements were made by the United States Attorney in the opening statement and in the

final argument. Certain excerpts from the argument are now quoted and are claimed to be erroneous. No exception was taken at the time these arguments were made by the appellant's learned counsel. The Court gave the usual and cautionary instruction that arguments of counsel are not evidence and not to be considered as evidence and are to be regarded by the jury only insofar as they agree with the jury's recollection of what the evidence was.

This case was long and lasted about three weeks. Testimony was voluminous. The defendants had five counsel part of the time and four during all of the trial. The case was tried in a vigorous manner and at times language was used on both sides that possibly was not the most courteous that could have been used. In view of the intricate issues involved and the length of the evidence, the arguments on both sides were surprisingly free from use of abusive and belligerent language and I believe there was only one or two objections in nearly a day and one-half of final argument.

Counsel for appellant Nemec in his final argument far exceeded the bounds of propriety and called for a vigorous answer. He stated as follows:

"I'm one of the men of Crescent City. My father was one also. If I felt, if I knew I'd been defrauded, I'd never be standing here now; I would have been in that witness chair talking as fast as the next witness." (Tr. 1859-1860)

Here counsel for the appellant Nemec stated to the jury that he and his father were investors in

Crescent City. He was arguing the case to the jury as well as testifying. Although the Government took no exception to this argument, Government counsel were entitled to reply to it in a vigorous and forthright manner and to comment upon the chain of evidence showing the fraud in strong vigorous terms and would be derelict in their duty for failure to do so.

APPELLANT DAWSON'S ASSIGNMENTS OF ERROR

The appellant Dawson's assignments of error will be discussed in the order in which they are set forth in the appellant's brief.

ARGUMENT

I. Answer to Appellant Dawson's Assignment of Error No. 1, viz., That the Verdicts are Contrary to the Law and the Evidence. The Evidence is Insufficient to Support the Verdicts.

The trial judge, in summing up the evidence as to Dawson on the Motion to Dismiss, summed up the case as follows:

"Mr. Redmond testified he met Mr. Dawson in September, 1945, and that's been gone into, as to what was done as to the employment of Mr. Redmond as an engineer for the Northwest Mining and Engineering Company. My notes show that Mr. Dawson told Mr. Redmond that he was an associate of Mr. Nemec in mining operations at Sierra City. Mr. Schnell saw Mr. Dawson and Mr. Nemec in 1946 and talked with them regarding the Mammoth Channel. He met them in a hotel in Chico, California. Mr. Smith met

Mr. Dawson near the operations of this Northwest Mining and Engineering Company in the spring of 1946 near Magelia, and Mr. Dawson asked about leasing the Genii Mine. Mr. Nemec was with Mr. Dawson at that time, and Mr. Dawson at that time told Mr. Smith that they were locating claims in the county, that they had located a group—no, that they were backed by a group of investors from Hanford. Mr. Dawson again talked with Smith in California in December, 1946 about the Genii Mine, and offered Mr. Smith at that time a job and a salary and an automobile if he would lease the mine and let Mr. Dawson have it. Of course, there isn't any evidence, as I understand it, definite evidence that he was leasing the mine for the Northwest Mining and Engineering Company, but the only association it is shown from the evidence that Mr. Dawson had, or the only reason he had to be in this particular area of California over a long period of time, was in some connection with Mr. Nemec's enterprise. There isn't any other evidence from which any other inference could be drawn.

“Mr. Helton saw Mr. Dawson, Rector and Nemec in California. Dawson told Helton he was a mining scout; he told him his company had joined forces with Dr. Rector, who was using his new knowledge gained at Hanford on the extracting of gold; then the newspaper article which Mr. Helton wrote, which he read back to Mr. Nemec, Rector and Dawson; and then of course there is Dr. Rector's testimony which has been gone into in considerable detail, and indicates that Mr. Dawson knowingly at least to some substantial extent entered into what Mr. Rector testified was a scheme or a plan to make it falsely appear that Dr. Rector was an atomic scientist and a nuclear physicist, and had been in an important position in connection with the government project at Hanford. Of course, reference has been

made to Dr. Rector's testimony, that he remarked to Mr. Dawson that he was fearful that it might become known that he was only a chiropractor, and Mr. Dawson replied 'Yes, that wouldn't do at all' and according to my notes Dr. Rector testified that at one time when he was acting as superintendent of the operations of the Northwest Mining and Engineering Company, that he, Dawson, and Nemec were all drawing checks on the bank account of the Northwest Mining and Engineering Company.

"That certainly would indicate that Mr. Dawson had a very direct connection with the operations of the Northwest Mining and Engineering Company, and then I won't refer in detail to the other evidence of Dr. Rector, and I am still of the view that where a witness's testimony may be weakened by contradictions or indications that at some time during his testimony he wasn't telling the truth, or where he changes his testimony from cross to redirect, that that matter is a matter of weighing or of judging the weight that should be given to the testimony, and that's for the trier of the facts, which is the jury in this case.

"Then Mr. Fegan, the Securities and Exchange attorney, testified that he had interviewed Mr. Dawson, and that Dawson said he had known Mr. Nemec for 25 years, and was working with him to set up this mining enterprise. Mr. Dawson wasn't of course definite; he said that he wasn't a partner, that he wasn't an officer of the company, but I have this note, that he said that he was associated with Frank Nemec, and that they would cut the pie when they had—at some stage of their proceedings, at any rate, would cut the pie. Now, from that I think there's ample evidence there to warrant submission of the case to the jury as to Mr. Dawson being a member of this conspiracy; and as to the other counts of the information, or rather the indictment, it has been held that a scheme devised to

use the mails to defraud is a conspiracy in effect, whether or not a conspiracy is specifically charged, and that the same rules of evidence apply, so that if one is a member of and participates in a scheme, and one of the members of that, a party to the scheme, does make a mailing, I might say this, that it must be a scheme that reasonably is of such a character that use of the mails will be required, and the mails are used by one who is in the scheme, that the others are bound by it, and I think it seems to me that it would be impossible to make a distinction here, that Mr. Dawson would either have to be considered a member of the conspiracy, I'm talking now of substantial evidence, if I leave him in the conspiracy I must leave him in the substantive counts, or he must be left out of all of them. I don't think there could be any distinction drawn between the first count and the later substantive counts." (Tr. 1154-1158)

Dawson did not make any sales. He was not employed by the Company for that purpose, but was engaged as a mining scout and a local manager who was to run the affairs of the Company locally. After the trial judge held there was enough evidence to hold Dawson as a defendant, the following additional evidence, submitted by the defendants, strengthened the case against Dawson by his acting participation:

Frederick H. Vahrenkamp testified he was engaged by Mr. Dawson as an engineer for the Northwest Mining and Engineering Company at Sierra City. (Tr. 1185) Dawson then proceeded to take the mining engineer, Vahrenkamp, to the operations at Sierra City, where they met the appellant Nemec. (Tr. 1185)

Dawson himself stated as follows in his own testimony:

“Q. Well, how were you to ‘cut the pie’ with Mr. Nemec, then?

A. Well, that phraseology of cutting the pie, it was mentioned I believe to an S. E. C. by the name of Newton in Los Angeles, if, as and when there’s a profit, then if Nemec was to cut the pie, then if that phraseology fits it, why, I was willing to take whatever slice that he was willing to give me.” (Tr. 1422)

Dawson later talked with Nemec about the Mammoth Channel properties and agreed to locate claims there for Nemec. (Tr. 1424-1425)

Dawson also admitted that he had told Nemec that he tried to make a deal with Elistes Hayes for the Sierra Butte Mine and failed. (Tr. 1450) He also tried to make a deal with High Pockets Smith for the Genii Mine, but failed. (Tr. 1451) He drew checks on the Northwest Mining and Engineering Company. (Tr. 1452) The evidence, as admitted by appellant Dawson in his brief, does show Dawson’s connection with the Northwest Mining and Engineering Company as a field representative, a man empowered to represent the Company in obtaining properties, leases, commitments, and even the power to write checks upon the company, although he did not go out in the field and make any sales of any claims or investment shares to any prospective purchaser. In any conspiracy case not all participants are salesmen, or managers, nor is it necessary that the appellant make a sale or be connected with all phases

of the work in order to hold him as a party to the fraudulent enterprise. If he participated, knowing of the fraud, aided and assisted in any way, he would be guilty. In this case, there was ample evidence to show that Dawson was an active principal throughout the fraudulent enterprise from the beginning at Sierra City, down to the returning of the indictment and that he was to "cut the pie" with the president of the Northwest Mining and Engineering Company, F. E. Nemec.

II. Answer to Appellant Dawson's Assignment of Error No. 2, viz., That the Court Erred in Permitting Evidence to be Received on the Theory of a Conspiracy on Both the Charges for Violation of the Securities & Exchange Act and of the Mail Fraud Statute. There was no Evidence Whatsoever to Support a Conviction on the Charge for Violation of Mail Fraud on the Part of the Appellant Dawson, and the Verdict Returned was on the Conspiracy Charge. Hence it Cannot be Told on What Basis the Jury Returned its Verdict."

The appellant Dawson lays considerable stress on the case of *Krulewitch v. United States*, 336 U. S. 440. The appellee has no quarrel with the *Krulewitch* case, which was a white slave traffic case in which the transportation was completed when the conversation as to the conspiracy took place. In the *Krulewitch* case the conspiracy had terminated and was no longer in existence as the offense had consisted of one transportation for immoral purposes. In this case the fraud was continuing down to the date of trial and the appellants were shifting from one min-

ing and manufacturing enterprise to another in order to garner every available dollar possible from the investors. This was a long trial lasting three weeks, the record comprising 2,679 pages and consisting of 215 exhibits. In this case the Government was compelled to build the case piece by piece. In other words, in the early stages of the trial certain exhibits, such as plaintiff's exhibits 49 and 63, were admissible as against one defendant and could not be connected up until later in the case.

As the trial judge pointed out, the Government was entitled to latitude, as it could not ask its questions of all of the different witnesses at once so as to make all evidence admissible against every conspirator at one time. It must proceed to build its case bit by bit and the defendants had an ample opportunity at the time the Government concluded its case to move for judgment of acquittal and did so. By that time the Government had made a *prima facie* case against appellants and the exhibits were then well connected. This procedure was approved by this court in the case of *Blumenthal v. United States*, (CCA 9) 158 Fed. (2d) 883, at page 891, also in the case of *Rose v. United States* (CCA 9) 149 Fed. (2d) 755. This court held the statements made by one conspirator during the conspiracy to further the objects of the conspiracy are binding on all conspirators.

The charge of conspiracy to violate the Securities Act and mail fraud statute in single count is permissible since the conspiracy is the gist of the of-

fense. *Braverman v. United States*, 317 U. S. 49, *Nye & Nissen v. U. S.* (CCA 9) 168 Fed. (2d) 846.

III. *Answer to Appellant Dawson's Assignment of Error No. 3, viz., That the Court Erred in the Admission of Plaintiff's Exhibit 211 as Being Highly Prejudicial to the Appellant Dawson on the Theory on Which the Case was Tried.*

Since a similar assignment of error is made as to the appellant Nemec, this assignment of error is discussed more adequately in the brief commencing at page 20. Plaintiff's Exhibit 211, which was a restraining order by the State of California prohibiting the appellant Nemec from selling securities in the State of California, was admitted as against appellant Nemec. It is believed that such exhibit could not be prejudicial to the appellant Dawson as he is not a party in any way to it.

IV. *Answer to Appellant Dawson's Assignment of Error No. 4, viz., That The Court Erred in Permitting Doctor Rector to Plead Guilty in the Presence of the Jury and then to Testify Against the Appellants in the Presence of the Jury.*

In the first place the record does not indicate that Dr. Rector did plead guilty in the presence of the jury. He pleaded guilty before a jury was impaneled to try the case. There were members of the jury panel present in court at the time, but the record does not so indicate. The matter of Dr. Rector's change of plea came as follows:

"MR. ETTER: At this time, your Honor, the defendant Rector waives the reading of the in-

dictment, desires to withdraw the plea heretofore entered in the other cause, I think 4166, and enter a plea of guilty to count one of the new indictment.

THE COURT: Where is Dr. Harold Rector?

MR. ETTER: Right here.

THE COURT: Mr. Erickson, do you have something to say to that? I assume you wouldn't object to that.

MR. ERICKSON: No, I wouldn't object if I could, and I have no objection to it.

THE COURT: Your name is Dr. Harold R. Rector?

DEFENDANT RECTOR: Yes, sir.

THE COURT: You understand the nature of the charge here?

DEFENDANT RECTOR: Yes, sir.

THE COURT: And have been fully advised as to your rights; it is your desire to withdraw your plea of not guilty to the former indictment in this case?

DEFENDANT RECTOR: I'm sorry—

THE COURT: I say, do you wish to withdraw the plea that you have heretofore entered of not guilty in the case?

DEFENDANT RECTOR: Yes.

THE COURT: All right; what say you now to count one of the indictment in this case, Dr. Rector?

DEFENDANT RECTOR: I wish to plead guilty.

THE COURT: All right, let the record show that Dr. Harold R. Rector has entered a plea of guilty in this case." (Tr. 24-26)

Objections were then made by Mr. Ulvestad, attorney for appellant Nemec, and Mr. Edgerton, attorney for appellant Dawson, that the procedure was in the presence of the jury. However, the jury had not yet been impaneled to try the case. They were impaneled later. (Tr. 27)

When counsel for Dr. Harold R. Rector approached the Court to ask permission to plead guilty, neither the Court nor other counsel had an idea of what he was going to do. The United States Attorney had a premonition that he might move to change his plea, but no assurance. In any event, it would be impossible to conceal the fact from the jury that Dr. Rector had changed his plea because even before the jury was impaneled and advised not to read anything in the newspapers, the newspapers had gone out with the story that Rector had entered a plea of guilty. He was mentioned in the indictment, which was a proper exhibit for the jurors to take to the jury room, and they could see his name in it. He was called as a witness on behalf of the Government—he testified in court against the co-defendants. The jurors at that stage of the proceedings certainly would know that he entered a plea of guilty as he was named in the indictment as a co-defendant. The fact that Dr. Rector entered a plea of guilty could not have been concealed from the jury with trials conducted openly and in public as they are under the American system of justice. This practice has been sanctioned in the case of *Grunberg v. United States*, (CCA 1) 145 Fed. 81, at p. 86.

V. Answer to Appellant Dawson's Assignment of Error No. 5, viz., That the Defendants were Prejudiced in Having a Fair Trial Guaranteed by the Fifth Amendment to the Constitution of the United States, in that Doctor Rector was an Admitted Perjurer and was Placed on the Witness Stand by the Government to tell one Story and then to Change his Testimony in the Very Presence of the Jury.

Certainly this assignment of error cannot be considered seriously. Appellant cites no cases to sustain his position. It is submitted that a single witness often gives contradictory testimony, that the weight of his testimony is for the trier of the fact, which is the jury. The fact is that his testimony changed during the time he was on the stand and was seized upon by the appellant Dawson's counsel and argued vigorously to the jury that they should disbelieve everything that he said. The court protected the appellant's rights thoroughly when the jurors were instructed that where a witness wilfully testified falsely as to any material matter of fact, the jury is at liberty to disregard that witness' testimony unless corroborated by other credible testimony. Appellant's argument goes to the weight of Rector's testimony rather than its admissibility. The Court gave the proper cautionary instruction. (Tr. 1918).

VI. Answer to Appellant Dawson's Assignment of Error No. 6, viz., That the Court Erred in Instructions Given.

Appellant's counsel at the time of the trial were satisfied with the instructions, as the trial court gave the instructions they asked for. No exception was

taken to the Court's instructions. (Tr. 1944) Therefore the instructions must be clearly erroneous and amount to a denial of due process of law to be considered now. No argument is made that they are such.

VII. *Answer to Appellant Dawson's Assignment of Error No. 7, viz., That the Court Erred in Instructing the Jury to Find as a Matter of Fact Whether the Partnership Agreements as Entered into Between the Appellants and the Alleged Victims were Within the Scope of the Securities & Exchange Act.*

In Title 15, Sec. 77 (b), Definitions, a security is defined as follows:

"(1) The term 'security' means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, pre-organization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a 'security,' or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing."

The appellant Dawson assigns as error that the court failed to instruct the jury as to whether or not the partnership agreements were securities within the meaning of the Act. Certainly the appellant cannot assign as error the failure of the court to instruct that these partnership agreements are securities. The

court defined what a security was and told the jury that it was for them to determine whether the interests offered were securities. It is submitted that there is ample evidence to support the jury's finding that the purchase contracts were securities, because they guaranteed each claim holder a participating interest in the net proceeds of the mining operations. The Court was extra cautious in appellant's favor in submitting the matter this way to the jury instead of instructing the jury that they were securities. Inasmuch as the securities in this case were similar to those involved and discussed in the case of *Securities & Exchange Commission v. Joiner*, 320 U. S. 344, the trial court followed the standards adopted by that case in proving whether or not these investment contracts were securities within the Act.

CONCLUSION

The ventures of these related operations of the Northwest Mining and Engineering Company were failures, as far as the investing public was concerned. They obtained nothing but pieces of paper entitling them to profits in the various enterprises, together with written and verbal assurances from the appellant, F. E. Nemec, that the profits would be available to them in short order.

The whole enterprise, therefore, consisted of a continuing scheme to sell to whoever was gullible enough to purchase any interest in any subsidiary of the Northwest Mining and Engineering Company, be it the Sierra City placers, Sierra City lodes, Sierra

City Mining Company, the Mammoth Channel claims, or the Crescent City Mining Company. Indeed, even at the time of the trial, the appellants were engaged in the manufacture of granium in Los Angeles, California, and at that time were promising the investors that they would soon attain success and have their money for them. The attempt of the appellants was to sell anyone any sort of a placer or lode claim, any of their operating companies, or any interest in any of their atomic processes to obtain money.

No effort was made by the Government to show how much of this money, or if any, was embezzled or stolen by the appellants. The whole theory of the Government's case was to show that the appellants and their agents made nineteen false and fraudulent representations as to the mining claims and enterprises to various investors and that the promises were false and known to the appellants to be false at the time they were made. The evidence also showed that the appellants used the mails from the beginning to the end of the scheme and, although the mailings were by the appellant Nemec, nevertheless appellant Dawson did know and could not have helped but know that the mails were used by the principal in this case. Dawson was a party to a continuing conspiracy and was responsible for substantive offenses committed by his co-conspirator, Nemec, although he may not have known of all of the substantive offenses. *Pinkerton v. United States*, 328 U. S. 640.

It is submitted that the record taken as a whole is remarkably free from error of any sort; that the only

exceptions taken in the whole case were as to the admissibility of certain exhibits which were later connected up with the defendants beyond any doubt and that the trial court was unduly solicitous in seeing that the defendants got a fair trial before an impartial jury under standards of fairness and justice which have been approved by this court and the highest court of the land.

Respectfully submitted,

HARVEY ERICKSON,
United States Attorney.

FRANK R. FREEMAN,
Asst. United States Attorney.
Attorneys for Appellee.



No. 11976

United States
Court of Appeals

for the Ninth Circuit

GRACE BROS., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of Record

Upon Petition to Review a Decision of The Tax Court
of the United States

FILED
SEP 23 1948

PAUL R. O'BRIEN, JR.

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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APPEARANCES

For Petitioner:

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BAYLEY KOHLMEIER, Esq.

For Respondent:

W. J. McFARLAND, Esq.

Docket No. 9766

GRACE BROS., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES

1945

Dec. 10—Petition received and filed. Taxpayer notified. Fee paid.

Dec. 11—Copy of petition served on General Counsel.

1946

Jan. 15—Answer filed by General Counsel. Copy served 1/18/46.

Jan. 15—Request for hearing at San Francisco, filed by General Counsel. Served.

Jan. 18—Notice issued placing proceeding on San Francisco, California calendar.

Oct. 4—Hearing set December 2, 1946—San Francisco, California.

Nov. 27—Joint motion for continuance filed. 11/29/46 Granted, next San Francisco Calendar.

1947

Feb. 24—Motion for leave to file the attached amended petition, amendment lodged, filed by taxpayer. 2/25/47 Granted.

Feb. 26—Copy of motion and amended petition served on General Counsel.

Mar. 19—Answer to amended petition filed by General Counsel. 3/21/47 Copy served.

Mar. 28—Hearing set May 26, 1947—San Francisco, California.

May 26, 27—Hearing had before Judge Johnson on merits. Stipulation of facts filed, (paragraph 18 has been deleted and also first sentence of paragraph 19). Petitioner's brief 7/11/47. Commissioner's brief 8/26/47. Reply brief 9/16/47.

June 23—Transcript of hearing 5/26/47 filed.

July 7—Brief filed by taxpayer.

Aug. 25—Brief filed by General Counsel.

Aug. 26—Petitioner's brief served on General Counsel.

Sept. 12—Reply brief filed by taxpayer. 9/15/47 Copy served.

1948

Jan. 27—Memorandum findings of fact and opinion rendered. Judge Johnson. Decision will be entered under Rule 50. Copy served 1/27/48.

1948

Mar. 1—Computation for entry of decision filed by General Counsel.

Mar. 4—Hearing set 3/31/48 on settlement.

Mar. 31—Hearing had before Judge Johnson on settlement. Not contested.

Apr. 5—Decision entered. Judge Johnson. Div. 10. [1*]

June 14—Petition for review by U. S. Circuit Court of Appeals, 9th Circuit, with assignments of error filed by taxpayer.

June 15—Proof of service filed.

June 21—Notice of filing petition for review with affidavit of service thereon, filed by taxpayer.

June 21—Statement of points filed by taxpayer with affidavit of service thereon.

June 21—Statement of evidence filed by taxpayer with affidavit of service by mail thereon.
6/24/48 Agreed to.

June 21—Designation of record filed by taxpayer with affidavit of service by mail thereon.
6/24/48 Agreed to. [2]

* Page numbering appearing at foot of page of original certified Transcript of Record.

The Tax Court of the United States
Docket No. 9766

GRACE BROS., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

AMENDED PETITION

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (symbols IRA:90D HVH & LB) dated September 20, 1945, and as a basis of this proceeding alleges as follows:

1. The petitioner is a corporation with principal office at 806 Donahue Street, Santa Rosa, California. The return for the period here involved was filed with the Collector for the First District of California.

2. The notice of deficiency (a copy of which is attached to the original petition and marked Exhibit A) [3] was mailed to the petitioner on September 20, 1945.

3. The taxes in controversy are declared value excess-profits taxes for the calendar year 1943 in the amount of \$10,740.53 and corporation excess profits taxes for the calendar year 1943 in the amount of \$136,103.60, consisting of a proposed deficiency in the amount of \$114,190.49 and a claimed overpayment in the amount of \$23,913.11.

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(1) The Commissioner erred in determining that the stock of wine sold by petitioner during the year 1943 was not a capital asset and that the gain derived from the sale thereof was ordinary income and not capital gain.

(1-a) The Commissioner erred in determining that the profit realized by petitioner from the sale of its winery business in 1943 was ordinary income and not capital gain.

(2) The Commissioner erred in failing to allow as a deduction the California Bank and Corporation Franchise Tax based upon the net income of petitioner for the calendar year 1943.

(3) The Commissioner erred in failing to determine that petitioner overpaid its corporation excess profits tax^{*} for the year 1943. [4]

(4) The Commissioner erred in including as taxable income in 1943 a capital gain from the sale of a winery and vineyard plant in the amount of \$99,002.64 since said sale occurred in 1944.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a) Petitioner is a corporation organized under the laws of the State of California and having its principal place of business in the City of Santa Rosa, State of California.

(b) Petitioner keeps its books and records and makes its income tax returns on the accrual basis of accounting.

(c) Prior to 1943 petitioner had been engaged among other things in the business of making and selling wines. In January, 1943, petitioner discontinued its business of making and selling wines and leased the buildings and machinery and equipment which it had used in the making of wine. At the time it discontinued the business of making wine petitioner had on hand 418,761 gallons of wine. During the year 1943 petitioner sold all of said wine for a total price of \$219,179.91. The cost to petitioner of said wine was \$79,046.33 and petitioner realized [5] a gain in the amount of \$140,133.58 from the sale thereof. All of said wine had been held by petitioner for a period of six months or more at the time of the sale thereof. Said wine constituted a capital asset and the gain realized from the sale thereof constituted long-term capital gain within the meaning of Section 117 of the Internal Revenue Code.

(c)-1. The sale of the wine as alleged in the preceding paragraph hereof was in fact a part of the sale by petitioner of its winery business including the intangible value of said business and the gain of \$140,133.58 treated by respondent as gain from sale of wine, was gain on sale of the intangible value of said winery business. **The said intangible asset and value of said winery business was established more than six months prior to the petitioner's sale thereof, so the entire profit realized thereon should be taxed as a long term capital gain. [6]**

(d) In determining its income and excess profits taxes for the year 1943 petitioner treated the gain

realized from the sale of said wine and winery business as long-term capital gain. In redetermining petitioner's net income and excess profits taxes for the year 1943 the respondent erroneously treated the gain from the sale of said wine and winery business as ordinary income, and as a result thereof erroneously overstated petitioner's declared value excess-profits tax liability and its corporation excess profits tax liability.

(e) On December 31, 1943, petitioner became liable to the State of California for a corporation franchise tax based upon and measured by petitioner's net income for the year [7] 1943. On December 31, 1943, said franchise tax accrued under the law of California and became a lien upon the real property of petitioner, which lien had the same force and priority as a judgment lien. In its California franchise tax return of its income for 1943, petitioner reported a franchise tax liability in the amount of \$9,385.03. Petitioner is informed and believes, and on the basis of such information and belief, alleges that as the result of adjustments in its income for the year 1943, as determined and made by respondent, its California franchise tax, based upon and measured by its net income for the year 1943, was and will be increased to the sum of \$12,-779.55. Petitioner failed to take any deduction in its income and excess profits tax returns for 1943 for any part of said franchise tax. In determining petitioner's net income and tax liability for the year 1943, respondent erroneously failed and refused to allow petitioner a deduction for any part of said

franchise tax based upon and measured by its net income for 1943.

(f) As the result of the errors hereinabove alleged, respondent overstated petitioner's [8] declared value excess-profits tax for the year 1943 by the amount of \$1,686.90 and overstated petitioner's corporation excess profits tax by the amount of \$136,103.60. Petitioner's declared value excess profits tax for the year 1943 did not exceed the sum of \$13,805.89 and petitioner's corporation excess profits tax for the year 1943 did not exceed \$16,823.19.

(g) Petitioner duly filed its corporation excess profits tax return for the year 1943 on or before March 15, 1944. In said return petitioner reported an excess profits tax in the amount of \$38,736.30. Said excess profits tax was duly paid by petitioner to the Collector of Internal Revenue for the First District of California during the year 1944. As a result of errors alleged herein and other adjustments made by respondent, petitioner overstated and overpaid its excess profits tax liability for the year 1943 by the amount of \$21,913.11. No part of said overpayment has been repaid or refunded to petitioner, and the entire amount thereof is now due, owing and unpaid.

(h) In the computation of the deficiency against which this petition is filed, the respondent treated the sale of wine and the sale [9] of the winery as occurring in the year 1943. In recognition of the fact that the sale of the wine and the winery was part of a continuing transaction which was com-

pleted in the year 1943, the petitioner did not contest the Commissioner's conclusion that the entire transaction was a 1943 transaction. However, in the event the Commissioner should contest that conclusion in this proceeding, the petitioner alleges that the sale of the winery did not take place until 1944 and the gain of \$99,002.64 resulting from that sale constitutes taxable capital gain in 1944 and the Commissioner was in error in including said gain in the year 1943.

Wherefore, petitioner prays that this Court may hear the proceeding, redetermine petitioner's net income for the year 1943, and determine that petitioner's declared value excess-profits tax for the year 1943 did not exceed \$2,752.26; that petitioner's corporation excess profits tax for the year 1943 did not exceed \$16,823.19; that petitioner overpaid its declared value excess profits tax and its corporation excess profits tax for the year 1943 by the aggregate amount of \$23,913.11; that the Court expressly determine, as a part of its decision, that said overpayment of \$23,913.11 was paid within two years before the mailing [10] of the deficiency notice herein; and grant such other and further relief as may be proper.

/s/ GEORGE H. KOSTER,

/s/ BAYLEY KOHLMEIER,

Counsel for Petitioner.

(Duly Verified.) [11]

EXHIBIT A

Treasury Department
Internal Revenue Service
74 New Montgomery Street
San Francisco 5, California

Sept. 20, 1945

Office of Internal Revenue Agent in Charge,
San Francisco Division
IRA:90-D HVH & LB
Grace Bros. Inc.
806 Donahue Street
Santa Rosa, California

Gentlemen:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1943 discloses an overassessment of \$10,-731.62 and that the determination of your declared value excess-profits tax liability for the year mentioned discloses a deficiency of \$10,740.53 and that the determination of your excess profits tax liability for the year mentioned discloses a deficiency of \$114,190.49 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington 25,

D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, San Francisco 5, California for the attention of Conference Section. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.,

Commissioner,

By /s/ F. M. HARLESS,

Internal Revenue Agent in Charge.

Enclosures: Statement, Form of Waiver, Claim.

STATEMENT

San Francisco IRA:90-D HVH & LB

Grace Bros. Inc.

806 Donahue Street

Santa Rosa, California

Tax Liability for the Taxable Year Ended

December 31, 1943

	Liability	Assessed	Over- assessment	Deficiency
Income tax	\$ 57,932.86	\$68,664.48	\$10,731.62	\$
Declared value excess-profits tax	15,492.79	4,752.26		10,740.53
Excess profits tax	152,926.79	38,736.30		114,190.49

In making this determination of your income, declared value excess-profits, and excess profits tax liability, careful consideration has been given to your protest dated May 28, 1945 and to the statements made at the conference held on June 11, 1945.

The overassessment shown herein will be made the subject of a certificate of overassessment which will reach you in due course through the office of the collector of internal revenue for your district, and will be applied by that official in accordance with section 322 of the Internal Revenue Code, provided that you fully protect yourself against the running of the statute of limitations with respect to the apparent overassessment referred to in this letter, by filing with the collector of internal revenue for your district, a claim for refund on form 843, a copy of which is enclosed, the basis of which may be as set forth herein.

A copy of this letter and statement has been mailed to your representative, George Koster, Esq., 300 Montgomery Street, San Francisco, California, in accordance with the authority contained in the power of attorney executed by you and on file in this office. [14]

Adjustments To Net Income

Net income for declared value excess-profits tax computation as disclosed by return.....	\$272,003.88	
Unallowable deductions and additional income:		
(a) Income from the sale of wine.....	\$140,133.58	
(b) Depreciation	6,138.74	
(c) Political contributions	250.00	146,522.32
		<hr/>
Total		\$418,526.20
Nontaxable income and additional deductions:		
(d) Capital gain	\$ 41,130.94	
(e) Capital stock tax.....	2,500.00	
(f) Cost of goods sold.....	3,052.55	
(g) California franchise tax.....	4,473.10	51,156.59
		<hr/>
Net income for declared value excess-profits tax computation adjusted		\$367,369.61

Explanation of Adjustments

(a) On your return form 1120 schedule "C" there was reported as a capital gain a profit of \$140,133.58, realized on the sale of your inventory of wine at the De Turk Winery, and computed as follows:

Sales proceeds	\$219,179.91
Cost of inventory.....	79,046.33
	<hr/>

Profit realized

\$140,133.58

Information submitted shows that this wine inventory constituted the stock in trade held by you at the De Turk Winery, for sale to customers in the ordinary course of business which was regularly and continuously carried on by you at the De Turk Winery; that the entire inventory was sold in one transaction to Garrett & Co. made pursuant to a written agreement executed on January 20, 1943. Under the terms of this written agreement the only asset sold was your wine inventory.

It is, therefore, held that the transaction did not constitute the sale of a capital asset, held for more than six months, under the provisions of section 117

of the Internal Revenue Code; and furthermore, it is held that the profit realized constituted ordinary income, taxable in full.

The profit of \$140,133.58 is therefore transferred from the schedule of total capital net gains and included herein as ordinary income. [15]

(b) The deduction of depreciation is decreased \$6,138.74 as disclosed by Exhibit A of this statement.

(c) The deductions claimed on your return include \$250.00 representing a contribution to a political campaign fund. Since this expenditure is not an ordinary and necessary business expense or an allowable contribution, the deduction claimed is disallowed.

(d) Reported gain of \$140,133.58 on the sale of capital assets is decreased \$41,130.94 as follows:

(1) Income from the sales of wine eliminated from capital gain	\$140,133.58
(2) Gain on the sale of winery and vineyard plant, omitted from return.....	99,002.64
	<hr/>
Decrease in capital gain.....	\$ 41,130.94

(1) Income from the sale of wine is held to be ordinary income as explained under item (a) of the foregoing.

(2) You failed to report income from the sale of a winery and vineyard plant. Capital gain on this transaction is included as follows:

Proceeds of sale December 31, 1943.....	\$150,000.00
Cost as disclosed by Exhibit B of this statement....	50,997.36
	<hr/>
Capital gain	\$ 99,002.64

(e) The deduction for capital stock tax is increased \$2,500.00 as follows:

Capital stock tax at \$1.25 per thousand on declared value of \$4,000,000.00 as of June 30, 1944, which accrued July 1, 1943.....	\$5,000.00
Amount claimed	\$2,500.00
	<hr/>
Increase	\$2,500.00

(f) On December 31, 1942 assets of the Grace Brothers Brewing Co. were distributed to the stockholders. You owned 51 per cent of the stock of the Grace Brothers Brewing Co. and 49 per cent of the stock was owned by Frank P. Grace Company. You received 51 per cent of said assets as a dividend and 49 per cent of said assets in a taxable exchange from the Frank P. Grace Company on the same date. In adjusting your 1942 income tax liability it was held that the value of the net assets was \$113,702.46 in excess of the value as reported by you. Your 1942 net income was increased as follows: [16]

Capital gain increased.....	\$ 54,740.76
Dividends increased	58,961.70

Total	\$113,702.46
-------------	--------------

The increase is due to increase in value of various assets as follows:

Cash	\$ 49.99
Accounts and notes receivable.....	723.92
Inventories	3,052.55
Stocks	54,091.29
Buildings	21,308.49
Machinery and Equipment.....	23,210.62
Automobiles and trucks.....	7,143.75
Furniture and fixtures.....	1,121.85
Land	8,000.00

Total assets	\$118,702.46
Less: Accounts payable assumed by you.....	5,000.00

Increase in net assets.....	\$113,702.46
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The increase in inventories of malt and hops is determined as follows:

Santa Rosa inventory revised.....	\$8,161.86	
As shown on return.....	6,800.00	\$1,361.86
Sacramento inventory revised.....	\$4,909.69	
As shown on return.....	3,219.00	1,690.69
Net increase in inventories at December 31, 1942.....		\$3,052.55

Such increase in inventories taken over December 31, 1942 constitutes an additional cost of goods sold in 1943, and an additional deduction is allowed there-
for.

(g) California franchise tax accrued during 1943, which is based on 1942 net income, is increased \$4,-026.29 as follows:

Increase in 1942 net income :	
Capital gain increased	\$ 54,740.76
Dividends increased	58,961.70
Total	<u>\$113,702.46</u>
Less :	
Capital stock tax increased.....	1,875.00
Net increase in franchise tax income.....	<u>\$111,827.46</u>
Franchise tax at 4 per cent on \$111,827.46.....	\$ 4,473.10

[Endorsed]: Filed Feb. 24, 1947. [17]

[Title of Tax Court and Cause.]

ANSWER TO AMENDED PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the amended petition in the above proceeding, admits and denies as follows:

1 and 2. Admits the allegations contained in paragraphs 1 and 2 of the amended petition.

3. Admits that the taxes in controversy are declared value excess-profits taxes and excess profits taxes for the calendar year 1943; denies the remaining allegations contained in paragraph 3 of the amended petition.

4 (1) and (1-a), (2), (3), (4). Denies that the determination of tax set forth in the notice of deficiency is based upon error as alleged in subparagraphs (1) and (1-a), (2), (3), and (4) of paragraph 4 of the amended petition. [34]

5 (a), (b). Admits the allegations contained in subparagraphs (a) and (b) of paragraph 5 of the amended petition.

(c) and (c-1)), (d), (e), (f), (g). Denies the allegations contained in subparagraphs (c) and (c-1), (d), (e), (f), and (g) of paragraph 5 of the amended petition.

(h). Admits that the respondent in his determination of the petitioner's tax liability treated the sale of petitioner's wine inventory and the sale of petitioner's winery as occurring in the year 1943; denies the remaining allegations contained in subparagraph (h) of paragraph 5 of the amended petition.

6. Denies generally and specifically each and every allegation in the amended petition not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ **J. P. WENCHEL**, PMM
Chief Counsel, Bureau of
Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel.
T. M. MATHER,
W. J. McFARLAND,
Special Attorneys, Bureau of
Internal Revenue.

[Endorsed]: Filed March 19, 1947. [35]

10 T. C. No. 21

The Tax Court of the United States

Grace Bros, Inc., Petitioner, vs. Commissioner of
Internal Revenue, Respondent.

Docket No. 9766

Promulgated January 27, 1948

FINDINGS OF FACT AND OPINION

1. A corporation, regularly engaged in the manufacture and sale of wine, sold its entire stock and leased its winery to the purchaser after its sole shareholder had decided to discontinue the business. The lease was cancelled the following year and the corporation sold the winery to a purchaser unconnected with the lessee.

(a) The evidence adduced, held, not to support a finding that any part of the consideration paid for the wine was applicable to the good-will of the business.

(b) Profit from the sale of the wine, held, ordinary income and not capital gain as the intent to discontinue the business did not convert stock in trade into a capital asset.

2. The California franchise tax imposed for the privilege of doing business in 1944, which tax is measured by income realized in 1943, held, not accrued and deductible in 1943. *Central Investment Corporation*, 9 T.C. 128.

George H. Koster, Esq., for the petitioner.

W. J. McFarland, Esq., for the respondent. [36]

The Commissioner determined deficiencies of \$10,740.53 and \$114,190.49 in petitioner's declared value excess profits tax and excess profits tax, respectively, for 1943, in part by treating as ordinary income a profit from the sale of its entire stock of wine, and by adding to income reported a capital gain of \$99,002.64 from the sale of its winery. No deduction was claimed or allowed for an amount paid in 1944 to California as a franchise tax. Petitioner contends that since it was in liquidation, its wine stock was a capital asset; that the profit from sale is taxable as a capital gain and that the franchise tax is deductible as accrued in 1943. The parties are now agreed that the winery was sold in 1944, and that the resulting gain is not taxable in 1943.

FINDINGS OF FACT

Petitioner, a California corporation with principal place of business at Santa Rosa, California, keeps its books on an accrual basis of accounting and filed its 1943 income tax returns, prepared on that basis, with the collector of internal revenue for the first district of California. In 1943 and for many years prior thereto it has engaged in various enterprises, including farming, grape growing and the manufacture and sale of wines and beer. It owned stock in other corporations, among them Grace Brothers Brewery of Los Angeles, the Fresno Brewing Company and the Santa Rosa Ice & Cold Storage Co. All of petitioner's stock was owned by its president and manager, Joseph T. Grace, of Santa Rosa, a man active in numerous civic, financial, industrial and agricultural enterprises, and for over twenty years a vice-president of the Bank of America.

In 1921 petitioner purchased a wine-manufacturing plant, long known to the trade as DeTurk Winery. It operated the plant until 1943, producing [37] from grapes grown by it or bought from others sweet and dry types of wine and some brandies which it sold to a regular clientele partly in bottles bearing the label "DeTurk Winery" and partly in barrels to wholesale customers who bottled and sold it under their own labels. "The DeTurk Winery, Established 1876" appeared above petitioner's name on its invoices. Petitioner's product was accepted by the trade as a wine of high quality; it was suc-

cessfully marketed, and the net profit from its sale for the years 1936-1942 was as follows:

1936	\$26,610.18	1939	\$16,100.84
1937	33,184.93	1940	10,459.86
1938	20,377.92	1941	7,995.20
		1942	18,959.53

In 1941 petitioner's sales were 157,518 gallons of dry wine in bulk and 8,888 gallons in bottles at an average price of 22.6 cents a gallon, and 46,943 gallons of sweet wine in bulk and 12,443 gallons in bottles at an average price of 37.2 cents a gallon. In 1942 it sold 114,046 gallons of dry wine in bulk and 7,028 gallons in bottles at 22.2 cents a gallon, and 46,009 gallons of sweet wine in bulk and 10,268 gallons in bottles at 36.8 cents a gallon. During the years 1936-1942 petitioner's average investment in this section of its business was \$150,000, of which roughly \$60,000 was attributable to the plant and \$90,000 to inventory. As dry wine should be held two years or more and red wine one year for aging, petitioner kept a substantial inventory in stock.

Finding his numerous activities excessive, Grace decided late in 1942 to discontinue the wine business, and petitioner limited its production for that year to 4,959 gallons extracted only from the grape supply grown by it, whereas normally its annual production was about 200,000 gallons. Nonetheless [38] it had an inventory of 522,761 gallons at the end of the year, produced in 1942 and prior years.

In November 1942 Grace advised L. A. Weller, an old acquaintance and vice-president of Garrett &

Co., Inc., of New York, that he intended to abandon the wine business. Weller manifested interest, asking the quantity of wine available for sale; saying that his firm's lease on a California plant was about to expire, and making inquiry about a lease of the DeTurk winery and the possibility of installing in it certain machinery. After Weller's return to New York, Garrett & Co. requested Grace by a telegram of December 28, 1942, to submit details if "interested in selling your inventory and leasing winery." Grace replied the following day "that we have several purchasers for our inventory and lease of winery and distillery"; offered specified quantities of several types of wine at 40, 55, 60 and 65 cents a gallon, respectively, and a lease "of winery, distillery and bonded warehouse" for five years at an annual rental of \$12,000. In further negotiation by telegraph, Grace inquired what part of the inventory was of interest, adding:

* * * anxious to close deal immediately to get
part of sales in this year income tax returns
* * *.

Agreement was reached by telephone and confirmed by a telegram of Garrett & Co. to Grace on December 31, 1942. By the contract Garrett & Co. agreed to purchase all petitioner's wine at 50 cents a gallon; to pay 20 per cent of the purchase price immediately, and to lease the winery for five years at \$10,000 annual rent. On the same day petitioner delivered 104,000 gallons; received \$52,000 therefor from Garrett & Co., and reported the profit on its 1942 income tax return. [39]

There remained 418,761 gallons of wine, carried on petitioner's books at \$79,046.33, consisting of 248,635 gallons of dry wine and 170,126 gallons of sweet wine. During 1943 petitioner made delivery of this entire stock, receiving \$124,317.50 for the dry wine and \$94,862.41 for the sweet wine. The price paid for the latter was by agreement somewhat in excess of 50 cents a gallon because 73,628 gallons contained a higher sugar content than required by California standards. Garrett & Co. also agreed to purchase 600 wine barrels from petitioner at \$4 each. On January 20, 1943, the parties signed a detailed memorandum of the agreement, setting forth its terms as above described, and on January 30 they signed the contemplated contract of lease. By its terms petitioner leased to Garrett & Co. the premises of the winery "together with all wine-making machinery and equipment located therein" and the right to use the spur track of a railroad on the east side of the property. The annual rental was fixed at \$10,000; the term of the lease at five years with right of renewal for an additional five years. The lessee agreed to keep the equipment in good working order and in a reasonable state of repair; it reserved the right to remove all machinery and equipment installed by it within sixty days of the lease's expiration. The lessor reserved a small office and the use of well water on the leased premises for its adjoining cold storage plant. It agreed to carry fire insurance except on equipment installed by the lessee, and in case of damage to make repairs

with due diligence. If the winery should be totally destroyed, the lease was to terminate.

In giving possession to Garrett & Co. petitioner surrendered its permit to manufacture and sell so that the lessee could procure a permit to operate [40] on the premises; turned over to the lessee all its wine stocks, cooperage and labels, its list of customers and its regular staff of eight or ten experienced employees. Thereafter neither petitioner nor Grace engaged in making or selling wines. Garrett & Co. paid petitioner rent under the lease to the end of April, 1944, when the parties terminated it by mutual agreement. On April 15, 1944, petitioner sold the winery to Taylor & Co. for \$150,000. Taylor & Co. was not a subsidiary of, or owned by Garrett & Co.

On or about March 15, 1944, petitioner filed a California Bank and Corporation Franchise tax return for 1943, indicating a tax due of \$9,385.03, which it paid in 1944. This tax was imposed for the privilege of doing business in the state in 1944, and was measured by income realized in 1943.

In computing petitioner's income tax, declared value excess profits tax and excess profits tax for 1943, the Commissioner determined (1) that petitioner realized ordinary income of \$140,133.58 from the sale of wine in 1943, and not a capital gain in that amount as reported by it; and (2) that petitioner realized a capital gain of \$99,002.64 from the sale of the winery. (3) Deduction of the California franchise tax for 1943 was neither claimed by petitioner on its return nor allowed by the Commissioner.

OPINION

Johnson, Judge: The parties are agreed that petitioner realized a profit of \$140,133.58 from the sale transaction with Garrett & Co., but petitioner assails the determination that this amount is taxable as ordinary income, advancing three contentions under which all or a part of such profit should be classed as capital gain and so taxed. [41]

First, it argues that despite the literal language of the sale contract and communications leading up to it, the sale was not of wine merely but also of the good will of the business. Grace testified that in his preliminary negotiations with Weller he offered to sell all the business and assets for \$375,000; that he arrived at this figure by assigning \$125,000 to the plant, \$150,000 to the stocks of wine and \$100,000 to good will, and that the price obtained for the wine was intended to cover good will. This price was \$271,179.91, inclusive of the \$52,000 received and reported in 1942. We cannot find such an offer upon the evidence adduced. In our opinion the telegrams affirmatively indicate that petitioner did not seek to sell the plant because in pressing Garrett & Co. for a decision, Grace wired that he had "several purchasers for our inventory and lease of winery and distillery"; while nothing in the interchange of communications even suggests an intention or offer to sell the winery.

In any event the actual transaction, not an unaccepted offer, is determinative of tax incidence, and even if Grace attempted to sell the plant and business as an entirety, that attempt would not color

the lease with the characteristics of a sale. Petitioner cites several cases to the general effect that a profitable business presumptively has good will, *Helvering vs. Security Savings & Commercial Bank* (C.C.A., 4th Cir.), 72 Fed. (2d) 875; [42] *White & Wells Co.*, 19 B. T. A. 416, and that when sold in its entirety, a part of the consideration paid is properly attributable to that good-will whether or not the sale contract so specifies. *Pfleggar Hardware Specialty Co. vs. Blair*, (C.C.A., 2nd Cir.), 30 Fed. (2d) 614; *Betts vs. United States*, 62 Ct. Cl. 1. Counsel stresses that in giving possession of the winery, petitioner turned over to Garrett & Co. its labels, list of customers and staff of experienced employees together with its existing stocks of wine, and we are asked to hold that in so doing it necessarily conveyed the goodwill of its business.

We should be impressed by this argument if there had been a sale, as in the cited cases, but under the facts here shown the advantages of whatever goodwill was inherent in petitioner's business passed to Garrett & Co. by lease, not by sale, and there is no controversy about the rental. In making the lease it is true that petitioner sold its entire stock of wines, but a sale of merchandise, particularly of goods that had been held as stock in trade, does not effect a conveyance of the seller's good-will. In phrasing his argument, counsel alleges "the transfer of petitioner's entire winery business", including goodwill of a value of \$100,000, and concludes that "therefore \$100,000 of the price received from Garrett & Co. should be allocated as the amount re-

ceived for the said intangible or going-concern value." But "the price received" was explicitly for wine, and we are not convinced by Grace's testimony that the amount of it exceeded the wine's fair market value by \$100,000 intended to cover goodwill. In the preliminary negotiations four different prices per gallon were quoted for four grades of wine, and the transaction was consummated on a compromise price [43] of 50 cents a gallon for all types and later adjusted upward slightly in respect of wines having a high sugar content. This method of price determination is wholly incompatible with the theory that something more than wine was being bought, nor can we believe that Garrett & Co. would have paid \$100,000 above market to obtain goodwill which it abandoned a little over a year later by cancelling the lease so that petitioner could sell the winery to Taylor & Co. Significantly petitioner offered no evidence of the market price of its grades of wine in December 1942 apart from Grace's general testimony that the price paid by Garrett & Co. was excessive by \$100,000. We are unable to make such a finding or to hold that the sale contract covered any more than its terms indicate.

Second, petitioner argues that "the transaction with Garrett & Co. involved the disposition of a unitary business as distinguished from particular assets, and therefore the entire profit from the transaction should be treated as a long-term capital gain." For the reasons above stated, we cannot accept petitioner's factual premise, and hence the legal arguments based on it become moot. The

“transaction” with Garrett & Co., we would point out, was not single, but comprised a sale of wine and barrels and the lease of a winery, and if it could be treated for tax purposes as a unit, the “profit from the transaction” would comprise not only the \$140,133.58 gain from the wines delivered in 1943, but also the undisclosed profit from the sale of wine in 1942, from the sale of barrels and from rents due under the five year lease which was prematurely terminated. These considerations point up the unsound character of petitioner’s contention, for under its own theory the entire proceeds of “the transaction” were not, and by their nature should not have been, reported on its income tax return for 1942. [44]

Third, petitioner contends that because of an intent to liquidate, followed by a “disposition” of the entire business, its wine stocks lost their character as stock in trade or property held for sale to customers in the ordinary course of business and became capital assets within the meaning of section 117(a)(1), Internal Revenue Code, so that all profit from their sale is taxable as a capital gain, and since the wine was held over six months (with exception of the 4,959 gallons produced in 1942), as a long term capital gain.

We are unable to agree with the view that Grace’s intention to liquidate converted petitioner’s stock in trade into capital assets and we hold here that the wine’s character as stock in trade was not lost and did not change by virtue of Grace’s decision to dis-

continue petitioner's wine business and by petitioner's sale of that stock in its entirety.

Petitioner cites *Three States Lumber Co. vs. Commissioner* (C.C.A., 7th Cir.) 158 Fed. (2d) 61, as to the contrary, but we are of opinion that by implication it strongly supports our conclusion. The taxpayer there terminated its business of cutting, sawing and selling timber in 1919, and then endeavored to sell its land, but without success until it began to sell parcels on the installment basis after 1930. Rejecting the Commissioner's contention that its profits were taxable as ordinary income, the Court held them capital gains because there was no evidence to

* * * support the conclusion that petitioner was engaged in business primarily for the purpose of selling land to customers in the ordinary course of its trade or business.

Inferentially if there had been such evidence, the profits would have been ordinary income notwithstanding liquidation. *Graham Mill & Elevator Co. vs. Thomas* (C.C.A., 5th Cir.), 152 Fed. (2d) 564, also cited by petitioner, even more strongly supports that view. The liquidating taxpayer there sold all its assets, including notes and accounts receivable, and on the latter it claimed [45] an ordinary loss deduction. But the Circuit Court of Appeals for the Fifth Circuit held the notes capital assets and the loss a capital loss because the taxpayer:

* * * was not in the business of selling notes and accounts, and had never so dealt with its notes and accounts before.

* * * They represented the taxpayer's business capital, but were not a part of his stock in trade.

Under such rationale it is to be inferred that liquidation brought about no change in the assets' classification and that if, as here, the taxpayer's normal stock in trade had been the subject of consideration, the decision would have been the reverse of what it was. We adhere to the view that an intent to discontinue business or to liquidate does not convert stock in trade into a capital asset, and sustain the Commissioner's determination that petitioner's profit from the sale of wine is taxable as ordinary income.

Petitioner assigned as error the Commissioner's inclusion in 1943 income of a capital gain of \$99,002.64 realized from its sale of the winery to Taylor & Co. The parties have stipulated that this sale occurred in 1944, and are agreed that the gain is not taxable in 1943.

On its tax return for 1943 petitioner did not claim **and** the Commissioner did not allow deduction of \$9,385.03, representing the California Bank and Franchise Corporation tax covering the year 1943, but paid in 1944. Petitioner contends that this tax is deductible as accrued in 1943. This issue was decided adversely to petitioner's contention in *Central Investment Corporation*, 9 T.C. 128, and adhering to that decision, we approve the Commissioner's action.

Reviewed by the Court.

Decision will be entered under Rule 50. [46]

The Tax Court of the United States
Washington

Docket No. 9766

GRACE BROS., INC.,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

This proceeding was called from the Hearing Calendar of March 31, 1948, for settlement under Rule 50. No appearance was made on behalf of petitioner, and the respondent's computation of tax filed on March 1, 1948, was not contested. Now, therefore, in accordance with said computation, it is

Ordered and Decided: That there is an overpayment in declared value excess-profits tax for the calendar year 1943, of \$240.04, which amount was paid within three years before the mailing of the notice of deficiency, which was mailed within three years from the time the return was filed by the taxpayer; and there is a deficiency in excess profits tax of \$124,073.01 for said year 1943.

(Seal) /s/ LUTHER A. JOHNSON,
Judge.

Entered Apr. 5, 1948. [47]

In the United States Circuit Court of Appeals
For the Ninth Circuit

Tax Court Docket No. 9766

GRACE BROS., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL
REVENUE,

Respondent.

PETITION FOR REVIEW BY THE UNITED
STATES CIRCUIT COURT OF APPEALS
FOR THE NINTH CIRCUIT

To the Honorable, the Judges of the United States
Circuit Court of Appeals for the Ninth Circuit:

Grace Bros., Inc., a corporation, by its attorneys
hereby petitions this Honorable Court to review
the decision of the Tax Court of the United States,
entered on April 5, 1948, finding a deficiency in
excess profits taxes paid by petitioner for the cal-
endar year 1943 in the amount of \$124,073.01.

I.

JURISDICTION

Petitioner is a corporation organized and existing
[48] under the laws of the State of California and
maintains its principal place of business in Santa
Rosa, California.

The excess profits tax return of petitioner for the
year 1943 was filed with the Collector of Internal
Revenue for the First Collection District of Cali-
fornia, in San Francisco, California, all within the

jurisdiction of the United States Circuit Court of Appeals for the Ninth Judicial Circuit.

The jurisdiction of this Court to review the decision of The Tax Court of the United States aforesaid, is founded on Sections 1141 and 1142 of the Internal Revenue Code.

II.

PRIOR PROCEEDINGS

On September 20, 1945, the Commissioner of Internal Revenue mailed a notice of deficiency in accordance with Section 272 of the Internal Revenue Code, proposing a deficiency in excess profits tax for the year ended December 31, 1943 in the amount of \$114,190.49. Petitioner duly filed its petition for redetermination of said deficiency in The Tax Court of the United States within the time provided by law. A hearing before the Tax Court was held in the City of San Francisco, California on May 26, 1947. The Tax Court promulgated its findings of fact and opinion on January 27, 1948, and the decision of the Tax Court determining a deficiency in excess profits taxes for said year in the amount of \$124,073.01 was entered on April 5, 1948. [49]

III.

NATURE OF CONTROVERSY

The controversy herein involves petitioner's correct excess profits tax liability for the year 1943, which in turn depends upon the determination of the following general issue:

1. Whether the gain, or any part thereof, realized by petitioner in 1943 from the sale of

its inventory of wine and its winery business is long term capital gain or ordinary income subject to excess profits tax.

Petitioner is a California corporation which was organized in 1910 and which maintains its principal place of business in Santa Rosa, California. In 1943 and for many years prior thereto petitioner was engaged in various business enterprises, including farming, cattle raising, manufacturing and selling ice, cold storage and manufacturing and selling beer. From 1921 to 1942 petitioner was also engaged in the business of manufacturing and selling wine under the trade name of The DeTurk Winery. The DeTurk Winery was built in 1876 and had been continuously operated at the same location by petitioner and the prior owners. The wine produced and sold under the name of The DeTurk Winery [50] was of better than average quality and enjoyed a good reputation. The operating staff of the winery also included valuable and well trained men.

Some time prior to October 1942 petitioner decided to go out of the winery business and to dispose of The DeTurk Winery. As the result of this decision petitioner limited its production of wine in the 1942 vintage season to the grapes grown by it and made efforts to sell the business.

In November or December 1942, Mr. Joseph T. Grace, the president and sole stockholder of petitioner, carried on negotiations and correspondence with Garrett & Co. through Mr. Weller, the vice-president, with regard to the sale of the wine and

winery business of petitioner to Garrett & Co. Mr. Grace advised Mr. Weller that petitioner would not sell its wine inventory unless it sold everything connected with the wine business, including the winery and the good will. At that time petitioner had an inventory of 522,761 gallons of wine and Mr. Grace further advised Mr. Weller that he thought the winery was worth \$125,000 and that the inventory and good will was worth \$250,000. Mr. Grace based his determination of \$250,000 for the wine and good will by estimating that petitioner could realize \$150,000 from the wine by continuing to sell it in the regular course of business and by estimating the value of the good will at five times the average annual net earnings of the wine business, making a good will value of \$100,000. [51]

After numerous conversations and telegrams, on December 31, 1942 Garrett & Co. offered to lease petitioner's winery and equipment for five years at \$10,000 annual rental and to purchase all of petitioner's wine at 50 cents per gallon. Petitioner accepted the offer and shipped 104,000 gallons that day. In 1943 petitioner transferred the balance of the wine, its bottles and cooperage, its DeTurk Winery labels, its permits to manufacture wine, its customer list, its winery personnel and possession of the winery to Garrett & Co. As the total price agreed upon was slightly greater than the price asked by petitioner, Mr. Grace considered that petitioner had sold the entire business, including good will, to Garrett & Co. and that petitioner had re-

ceived \$100,000 for the good will of the winery business.

In its income tax return and its excess profits tax return for 1943 petitioner treated the sale as a sale of capital assets held for more than six months and reported a long term capital gain in the amount of \$140,133.58. Respondent treated the gain from the sale as ordinary business income and thereby substantially increased petitioner's net income subject to excess profits tax and substantially increased petitioner's excess profits tax liability for 1943.

In its appeal to the Tax Court petitioner presented the following contentions:

1. The transaction with Garrett & Co. involved the disposition of a unitary business as [52] distinguished from particular assets, and therefore the entire profit from the transaction should be treated as long term capital gain and taxed accordingly.

2. When petitioner decided to discontinue making wine and to dispose of the winery business, the wine on hand ceased to be held for sale to customers in the ordinary course of petitioner's business, and became a capital asset, and having been held for more than six months (except the 4959 gallons manufactured in 1942) the gain constituted long term capital gain.

3. In any event at least \$100,000 was received by petitioner for its good will which was unquestionably a capital asset and therefore at least \$100,000 of the gain was long term capital gain realized from the sale of the good will.

The Tax Court determined that transaction be-

tween petitioner and Garrett & Co. was not a disposition of the business as a unit and further determined that since the winery was leased and not sold to Garrett & Co. and since the price was determined on the basis of 50 cents per gallon for the wine, the sale did not cover anything but wine, that the wine was not converted into a capital asset and that no part of the consideration received by petitioner was received for good will or other intangible assets. The Tax Court affirmed the determination of respondent. [53]

IV.

ASSIGNMENTS OF ERROR

In making and rendering its decision, as aforesaid, The Tax Court of the United States erred to the prejudice of petitioner in the following respects:

1. In determining a deficiency in petitioner's excess profits tax for the calendar year 1943 in the amount of \$124,073.01.

2. In failing to determine that there was no deficiency in excess profits tax due from petitioner for the year 1943 and that petitioner overpaid its **excess profits tax** for said year by the amount of at least \$23,913.11.

3. In determining that the stock of wine sold by petitioner during the year 1943 was not a capital asset and that the gain derived therefrom was ordinary income and not capital gain.

4. In determining that the transaction with Garrett & Co. did not involve the disposition of a unitary business, as distinguished from particular assets, the profit from which should be treated as long term capital gain.

5. In determining that no part of the consideration received by petitioner for its wine and other assets connected with its winery business was received for the good will of said winery business.

6. In failing and refusing to determine that at least \$100,000 of the consideration received by petitioner for its wine and other assets connected with the winery was received by petitioner for the good will of petitioner's winery business.

7. In failing and refusing to accept the uncontradicted testimony of the president of petitioner that the petitioner sold its good will and that the consideration received by petitioner upon the sale of its wine and other assets of its winery business exceeded the fair market value of the tangible assets sold by at least \$100,000 and that said \$100,000 represented consideration received by petitioner for the good will of its winery business.

Wherefore, petitioner prays that the decision of The Tax Court of the United States be reviewed by the United States Circuit Court of Appeals for the Ninth Circuit and that a transcript of the record be prepared in accordance with the law and with the rules of said Court and transmitted to the Clerk of said Court for filing, and that appropriate action be taken to the end that the errors complained of be reviewed and corrected by said Court.

/s/ GEORGE H. KOSTER,

/s/ BAYLEY KOHLMEIER,

Attorneys for Petitioner.

(Duly Verified.)

[Endorsed]: T.C.U.S. Filed June 14, 1948. [55]

[Title of Tax Court and Cause.]

NOTICE OF FILING PETITION FOR
REVIEW

To: Charles Oliphant, Chief Counsel, Bureau of
Internal Revenue.

You are hereby notified that Grace Bros., Inc., did, on the 14th day of June, 1948, file with the Clerk of The Tax Court of the United States, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Ninth Circuit, of the decision of this Court heretofore rendered in the above entitled case. Copy of the Petition for review as filed is hereto attached and served upon you.

Dated this 15th day of June, 1948.

/s/ VICTOR S. MERSCH,
Clerk, The Tax Court of the
United States.

Service of copy of Petition for Review acknowledged this June 15, 1948.

CHARLES OLIPHANT,
Chief Counsel, Bureau of Internal Revenue, Attorney for Respondent.

[Endorsed]: Filed June 15, 1948. [57]

[Title of Tax Court and Cause.]

NOTICE OF FILING PETITION FOR
REVIEW

To: Honorable Charles Oliphant, Chief Counsel,
Bureau of Internal Revenue, Washington, D. C.

You Are Hereby Notified that on June 14th of 1948, a Petition for Review by the United States Circuit Court of Appeals for the Ninth Circuit of the decision of The Tax Court of the United States heretofore rendered on April 5, 1948 in the above-entitled cause was filed with the Clerk of The Tax Court.

A copy of said petition so filed is attached hereto and served upon you.

/s/ GEORGE H. KOSTER,
/s/ BAYLEY KOHLMEIER,
Attorneys for Petitioner.

(Affidavit of Service by Mail attached.)

[Endorsed]: Filed June 21, 1948. [58]

[Title of Tax Court and Cause.]

STATEMENT OF POINTS TO BE RELIED
UPON ON APPEAL

Comes now the petitioner above named, by its attorneys of record, and states that it intends to rely on appeal on all and each of the errors assigned in the Petition for Review herein, and petitioner

hereby formally adopts the errors assigned in the Petition for Review as its Statement of Points to be Relied Upon on Appeal.

/s/ GEORGE H. KOSTER,
/s/ BAYLEY KOHLMEIER,
Attorneys for Petitioner.

(Affidavit of Service by Mail attached.)

[Endorsed]: Filed June 21, 1948. [60]

[Title of Tax Court and Cause.]

STATEMENT OF EVIDENCE

The following is a statement of all the evidence submitted to The Tax Court of the United States in the above-entitled cause which is material and necessary for the determination of the assignments of error set out by the petitioner on review in its petition for review by th Circuit Court of Appeals for the Ninth Circuit of the decision of The Tax Court of the United States.

The above-entitled cause came on for hearing at San Francisco, California before the Honorable Luther A. Johnson, Juge of The Tax Court of the United States on May 26th and 27th, 1947. George H. Koster appeared on behalf of petitioner and W. J. McFarland appeared on behalf of respondent.

After the opening statement by counsel for the parties, there was offered and received by the Tax Court a Stipulation of Facts with exhibits attached thereto.

Thereupon, there was offered and received in evidence the following exhibits:

Respondent's Exhibit A—The tentative corporation income and declared value excess profits tax return of Grace Bros., Inc., for the year 1942.

Respondent's Exhibit B—The final corporation income and declared value excess profits tax return of Grace Bros., Inc. for the year 1942.

Respondent's Exhibit C—The tentative corporation excess profits tax return of Grace Bros., Inc. for the year 1942.

Respondent's Exhibit D—The final excess profits tax return of Grace Bros., Inc. for the year 1942.

Respondent's Exhibit E—The tentative corporation income and declared value excess profits tax return of Grace Bros., Inc. for the year 1943.

Respondent's Exhibit F—The final corporation excess profits tax return of Grace Bros., Inc. for the year 1943.

Respondent's Exhibit G—The tentative excess profits tax return of Grace Bros., Inc. for the year 1943.

Respondent's Exhibit H—The final excess profits tax return of Grace Bros., Inc. for the year 1943.

Thereupon,

MR. A. R. MORROW

was called as a witness by petitioner and having been duly sworn testified as follows: [63]

Direct Examination

By Mr. Koster:

My present business address is 900 Minnesota Street, San Francisco, California. For the past 55

(Testimony of A. R. Morrow.)

years I have been engaged directly or indirectly in the manufacture and sale of wines and have been and now am an officer of Fruit Industries, Ltd., one of the largest cooperative organizations in California making and selling wine. In my position with that organization I supervised the manufacture and blending of wine by the various members of that organization. During the years that The DeTurk Winery, operated by Grace Bros., Inc., was in operation I was consulted frequently on the blending of the wines produced by The DeTurk Winery. I am thoroughly familiar with the business and quality of the wines and brandies produced by The DeTurk Winery.

I have for many years been engaged in classifying wines. In classifying wines you determine the alcohol, acids, color and general quality of the goods. If you are buying you pay on those classifications. That has been my end of the game for the last 55 years. My classifications have been accepted by many different persons engaged in the wine industry and wines have been purchased and sold on the basis of those classifications.

In my opinion The DeTurk Winery has always had the reputation of handling the very best wines. Of course they had some inferior as well but since Mr. Grace has owned the plant I have helped him supervise the handling and manufacturing and blending of his wines to meet certain standards which have been above average. [64]

(Testimony of A. R. Morrow.)

In the conduct of my work I have had occasion to learn the general reputation of The DeTurk wines in the wine industry and that reputation is good.

Q. (By Mr. Koster): In your experience, Mr. Morrow, have you ever reached a conclusion as to the value of a winery business insofar as it is related to the type of product and the quality of the product produced by that winery?

A. Well, I only—this is my only idea—my idea would be a fair value would be about five times the net proceeds of the wine, or in that neighborhood. I don't say it exactly.

Q. Do you believe that a winery producing a quality of wine that is above average has a value to its business in excess of the value of the tangible assets employed in that business?

Mr. McFarland: I object, if the Court please. My objection goes to their line of questions. I say it is no different from the previous ones and not rendered any the less objectionable.

The Court: The question is whether or not this witness knows by reason of his long association with the winery business whether or not different brands of wine affect the value of the wine, as to whether it is true or not.

The Witness: It does affect the value.

The Court: Above its ordinary intrinsic value on account of the brands?

The Witness: The brands, and also the quality of the wine.

(Testimony of A. R. Morrow.)

The Court: You know from your business experience that that is true, do you?

The Witness: Yes, sir. [65]

The Court: And from knowledge and observation of what has been going on? Do you know that from what you have seen?

The Witness: Yes.

The Court: I think the witness is qualified.

Q. (By Mr. Koster): I will ask the question again: Do you believe that The DeTurk Winery business conducted by Grace Bros., Inc., had a value, an intangible value, in excess or over and above the value of the tangible assets employed in the making and selling of that wine?

A. I do.

Cross Examination

Upon cross examination by Mr. McFarland, Mr. Morrow testified as follows:

Q. (By Mr. McFarland): Mr. Morrow, have you ever evaluated the good will or intangible value of a winery for any particular purpose other than your own purpose?

A. No, I have not.

Q. You know nothing of the problems presented in that connection? A. No.

Q. Now you have testified as to the value of a clientele or build-up by product of wine of any particular winery over and above its tangible value, as I understand it, in this connection. Have you made an investigation as to the tangible value of the Grace Bros. Winery in Santa Rosa?

(Testimony of A. R. Morrow.)

A. I have. I assist Mr. Grace in handling the blending and manufacturing of his wines, through my advice.

Q. Over the years?

A. Yes. We used to own The DeTurk Winery—the California Wine Association—and we originally sold it to Mr. Grace and I helped him [66] along wherever I could to advance his quality and sales and anything pertaining to the business.

There being no further questions Mr. Morrow was excused.

Thereupon,

MR. JOSEPH T. GRACE

was called as a witness by petitioner and having been duly sworn testified as follows:

Direct Examination

By Mr. Koster:

The tax liability shown on the income tax return of Grace Bros., Inc. for the year 1943 was paid as follows: March 15, 1944, \$9,000.00; May 15, 1944, \$9,354.19; June 15, 1944, \$18,354.19; September 15, 1944, \$18,354.18; December 15, 1944, \$18,354.18; making a total payment for that year of \$73,416.74.

The tax liability shown on the excess profits tax return of Grace Bros., Inc. for the year 1943 was paid as follows: March 15, 1944, \$15,000.00; June 15, 1944, \$4,368.15; September 15, 1944, \$9,684.08; December 15, 1944, \$9,684.07; making a total payment for that year of \$38,736.30.

(Testimony of Joseph T. Grace.)

The tax liability shown on the California franchise tax return for the income year 1943 was paid as follows: March 15, 1944, \$2,000.00 May 15, 1944, \$2,692.52; September 15, 1944, \$4,692.51; making a total of \$9,385.03.

My address is Santa Rosa, California. I am President of Grace Bros., Inc., the petitioner in this case, and have been President of the company since about 1930. Prior to that time I was Vice-President. My brother died in 1930, I think, and after his death I was made President. I own and control practically all the stock of Grace Bros., Inc. [67]

I am President and a director of Joseph T. Grace Farms, Inc., which is operating farms in Mendocino County. I am President of Grace Bros. Brewery, Ltd. in Los Angeles, which makes beer in Los Angeles and has a substantial business. I am President of Buffalo Brewery at Sacramento, which operates a brewery in Sacramento and has a substantial business. I am President of the California Ice Co. of Oakland, which makes ice in the City of Oakland. I am Vice-President of the Bay Cities Ice Co. in San Francisco, which makes ice to supply the trade in San Francisco. I am President of the Santa Rosa Ice and Cold Storage Co. which operates a cold storage plant at Santa Rosa and supplies ice to the trade. I am a director of the Bay Area Council that has to do with the nine counties that border on San Francisco Bay, and whose purpose is the advancement of those nine

(Testimony of Joseph T. Grace.)

counties. We have lately been putting in most of our time trying to decide the best place or proper place to locate the second bridge from San Francisco to Oakland. I am a director of the State Board of Agriculture. I am a director of the California State Fair Association. I am President of the Sonoma County Fair.

For twenty years I was Vice-President in charge of bank activities north of the Bay for Bank of America. I am now a member of the Bank's Advisory Committee. I am not as active with the Bank as I used to be although I take part in supervising their loans at their bank in Santa Rosa and their Healdsburg Branch at Healdsburg. Most of the time when I was actively associated with the Bank I had charge of the Bank's branches north of the Bay up to Lake County and Mendocino County. I visited those branches at intervals and checked into the activities of the branch and the loans particularly and other things that would have to do with the operation of the branch. I had occasion to review loans to determine the extent of the [68] risk involved in the loans. I had occasion to analyze statements submitted by persons asking credit. I had occasion in those investigations to determine the future earning power of any companies or any business enterprise seeking credit or extension of credit.

Q. (By Mr. Koster): Have you ever had occasion in your experience in that regard to determine

(Testimony of Joseph T. Grace.)

the value of the future earning power in so far as the determination of risk on your extensions of credit was concerned?

A. Well, I don't just quite understand you, Mr. Koster. You mean as to the value as it relates to—

Q. To any organization seeking credit as it relates to future earning power.

A. Well, yes. Those are always considered, the relation to the application for any loan that may be made to the earning power of the corporation or the individual to see that he has the earning power to repay the loan within a time, reasonable time, according to the business that he may be engaged in.

Q. Did you consider any other factors in connection with the organizations' setup of any companies or business enterprises seeking extensions of credit?

A. Well, frequently people would come or organizations would come in to seek a loan and they would ask or tell the purpose for which the loan was to be used. Then we would either encourage them or approve it or discourage it if we didn't think it was based on the right foundation.

Q. Did you ever consider the reputation of the management or the business in that regard?

A. Of the management?

Q. Did you ever consider the reputation of the management or the business in that regard?

A. Always. [69]

In 1943 and prior years Grace Bros., Inc. had an interest in several farms. Prunes were about the

(Testimony of Joseph T. Grace.)

biggest crop or one of the biggest crops. We raised prunes and sheep, hops, pears, grapes and the company also had an interest at that time in the Grace Bros. Brewery in Santa Rosa and also in Grace Bros., Ltd. in Los Angeles. I think also in the ice and cold storage business in Santa Rosa.

Grace Bros., Inc. owned some of the property which it farmed and some of the property was leased. Grace Bros., Inc. raised some grapes and operated The DeTurk Winery.

Grace Bros., Inc. acquired The DeTurk Winery about 1921 and operated it until the sale. The winery was built by Mr. Isaac DeTurk about 1876 and upon Mr. DeTurk's death it passed to some other hands and we bought it in 1921. We called it The DeTurk Winery because it was always known as The DeTurk Winery and always operated as The DeTurk Winery. The general business activity of The DeTurk Winery was making and selling sweet and dry Wines. The wine was sold at retail and also at wholesale. We sold the bottled wine to stores who resold it and we sold the wine to restaurants and other places bottled. We sold some of it in barrels to concerns which bottled the wine under their own label. We used the "The DeTurk Winery" label on our own sales bottled. We sold it wholesale to "vintners", a class of people in the wine trade who buy wines that they like and bottle them under their own brands. We sold wine to several of those men engaged in that business under their own label. We continued to sell to the same

(Testimony of Joseph T. Grace.)

class of customers every year since we started operating The DeTurk Winery. I think we might have lost a customer occasionally but we held on to our trade pretty well and we added some new ones as we went along, but we kept pretty much to the same class of trade. [70]

Some of the grapes from which we made the wines were grown by the company and some were purchased from grape growers in the district of Sonoma County and we bought some grapes from outside and shipped them in during the season.

It is necessary to age wine for a period of time before it is salable. Dry white wine should be at least two years old before it is bottled and dry red wine should be a year. Sweet wine on account of the higher alcohol content does not require the age, although age will improve it.

Q. (By Mr. Koster): Do you know how much wine was produced by The DeTurk Winery in the years 1936 to 1942?

A. Well, we produced some brandy in that year too, which I overlooked a few moments ago. In 1939 I think we produced quite a bit of brandy and we made approximately 200,000 gallons of wine a year, I would say.

Q. Mr. Grace, it is stipulated that in the year 1942 The DeTurk Winery produced 4,959 gallons of wine. Is that less than what the winery usually produced?

A. Oh, yes. Considerably less.

(Testimony of Joseph T. Grace.)

Q. And why did The DeTurk Winery produce that smaller quantity of wine in that year?

A. Well, we had decided to go out of the wine business.

Q. When did you make that decision?

A. Along in '42, I think.

Q. What month or what part of the year?

A. Well, it was before the vintage because we decided we wouldn't make—the only wine we made in '42 was from the grapes that the company had on its own ranches. We crushed those, but we decided on account of [71] our decision to go out of the wine business and the fact that we had a pretty good stock on hand also, that we would only make up the grapes that we owned ourselves.

Q. Mr. Grace, did you actively manage all of the business affairs of Grace Bros., Inc.?

A. Practically.

Q. Did you make any effort in 1942 to dispose of The DeTurk Winery business?

A. Well, I know that we had it in mind that eventually we would go out of the business. We decided to do that about along towards the end of '42.

Q. Did you make any effort to sell your winery business? A. Yes.

Q. Did you offer it for sale at any time?

A. Yes, I talked to different people on it, about the sale of the winery, and the stock of the wine, and everything that had to do with the winery. We had a very good organization in the winery,

(Testimony of Joseph T. Grace.)

men that had been with me for a good many years, and naturally I was anxious to so arrange a sale that these men would have a job and have work to continue. They had been very faithful and loyal.

Q. When did you first meet Mr. Weller, representative of Garrett and Company?

A. I met Mr. Weller, Oh, I met Mr. Weller first maybe ten or fifteen years ago. That is, I have known him for a long time.

Q. Did you meet him at any time in connection with any negotiations with respect to the sale of the DeTurk Winery? [72]

A. Yes. I met Mr. Weller in Fresno.

Q. When did you meet him there?

A. Well, it was just a short time before we made the sale.

Q. What month and what year?

A. That was in November, I would say, the latter part of November or early in December.

Q. Of 1942? A. 1942.

The Court: You mean when you met him or when you made the sale?

The Witness: No, that is when I met him, your Honor, and we discussed it. As I recall the conversation, he said, "I hear you have some wine to sell," and I told Mr. Weller that that was right, that we were going out of the wine business.

I also told him that we had a winery and that I wouldn't sell the wine inventory unless I sold everything in connection with the wine business, that is, winery and the wine inventory and the good

(Testimony of Joseph T. Grace.)

will in it—everything that had to do with it, and that we wanted to get out of the business. We discussed things a little bit. He asked me about how much wine we had and I remember I told him. He asked me what our ideas were and what we wanted. I told him I thought the winery was worth \$125,000 and I told him that the wine inventory and the good will, in my opinion, was worth \$250,000. That would be \$375,000 for everything. I impressed on him at the time, too, that we had a good organization and I was anxious to have those men taken care of. They were later taken over by Mr. Weller.

The Court: As I understand it, Mr. Weller was acting for Garrett and Company? [73]

The Witness: Mr. Weller was acting for Garrett and Company. He is Executive Vice President.

The Court: Vice President of the Company?

The Witness: Vice President of the Company, yes, your Honor.

Q. (By Mr. Koster): When you quoted the price of \$250,000 for the wine inventory and everything that went with it, did you make any computation to arrive at that figure?

A. Yes. I figured at the rate we were selling the wine at our current prices, that we should get out of it about \$150,000—somewhere in that neighborhood—and there would have to be some expenses maybe taken out of that for operating, so that I figured if I could get, when I asked \$250,000, that I would get the current value of the wine inventory

(Testimony of Joseph T. Grace.)

and there would be \$100,000 for the good will which I valued very highly.

Q. Did you conclude any final deal with Mr. Weller at that time?

A. Well, I think he said he would see about it and I think it was a few days after—it might have been a week or so—we had another meeting and he said, “Now, Mr. Grace, I would like to lease your winery for a while. I think I would like to lease the winery instead of buying it until I find out for sure that it is going to suit us.”

He said, “The lease I have at Healdsburg,”—which is just 16 miles north from Santa Rosa—“on my concentrator”—(Garrett and Company had been buying grapes from Healdsburg and making them into a grape juice, a grape syrup, which was a concentrated form of grapes and they shipped that grape syrup east and then added a certain amount of water and other things to it and made wine of it)—he says, “My lease at Healdsburg is out or will be out in a few months and I want a place where I can move my concentrator.” [74]

I was familiar with the concentrator and I knew that you have to have very large boilers to operate the concentrator because it requires a lot of steam. So when he talked about leasing the winery and agreed to move his concentrator there and take a lease of the winery, I figured that that was tantamount to a sale, because I didn't see how he could afford to move all of that machinery or install all of that machinery at the winery at Santa Rosa and

(Testimony of Joseph T. Grace.)

not buy the winery. The investment as I figured would cost him \$50,000. So that I felt that a lease to him was tantamount to a sale of the winery to him.

Well, it went on for a while and he put in the concentrator at Santa Rosa and he put in the big boilers. Then he said he thought he might like to—there was a winery up the valley further in Mendocino County that might suit him.

Q. At the time, just so we might have this in chronological order here, at the time he discussed with you the matter of leasing the winery, did you also discuss with him the matter of purchasing the wine and other assets?

A. Oh yes, he did. He said, "I can give you what you ask for your wine inventory and everything that goes with it, the good will, which would be equivalent to \$250,000." He says, "If I give you 50 cents a gallon, that will give you what you are asking."

And it give us, as a matter of fact, about \$10,000 more than we were asking. So that I felt we were getting the price that we were asking for the good will, the organization and all that, which went over to Mr. Weller later. We delivered him all those intangibles, all the good will things we had in mind—they were delivered to the Garrett people. [75]

Q. And did those negotiations result in the agreement of January 20, 1943? A. It did.

Q. Between yourself and Garrett and Company?

A. That's right.

(Testimony of Joseph T. Grace.)

Q. And I might say that that agreement is attached as an exhibit to the stipulation of facts.

When you concluded the negotiations, did you transfer to Garrett and Company your winery organization? A. We did.

Q. Employees? A. We did.

Q. After the negotiations were completed, just what took place?

A. The key men—in a winery there are certain departments to the winery—some men have to do with the crushing of the grapes and the making of the wine; other men have to do with the clarifying of the wine and the storage of it and the bottling of it. I am very sure that all of the organization, all of the key men remained in and many of the other men, but during the crushing season we have a lot of what we call “casual help” that come in for maybe the vintage season of maybe three or four weeks. Of course, they were gone, but the real valuable men we had trained for many years in the art of wine making, they remained with Garrett.

The Court: Was that part of the agreement that they were to remain or did they just remain?

The Witness: No, that was part of the agreement that we should do what was necessary to turn them over. We talked to them and the men all decided to remain with Garrett and Company. [76]

Q. (By Mr. Koster): What happened to all of the winery equipment and bottles and barrels and labels?

(Testimony of Joseph T. Grace.)

A. Well, the labels were taken over by Garrett and Company. They were delivered to Garrett and Company. The bottles, I don't know, for sure, I think we, knowing of the sale, I think we had reduced our stock of bottles pretty well, but we turned all of the labels over to Garrett and Company.

Q. Mr. Grace, what happened to it—what did you do with respect to—how did you inform your customers as to this transaction with Garrett and Company?

A. We informed the customers we had sold out to Garrett and Company, and we asked them to send their orders and to patronize Garrett and Company.

Q. Now, when did the matter of the actual sale of the winery plant first come into discussion?

A. You mean the winery, the building?

Q. As I understand it, Garrett and Company leased the plant under the agreement of January 20. How long did they lease it?

A. They leased the plant and operated it for one year, one season, and they—I think about 14 months, into April of the following year.

Q. What followed?

A. Mr. Weller came to me saying there was a winery up country that might be better situated for the needs of his business and would we release him from the lease. I said, "Well, Mr. Weller, if we could sell the winery I think we would release you."

A short time after the Taylor people appeared,

(Testimony of Joseph T. Grace.)

within maybe a few weeks. The Taylor people appeared and opened negotiations for the purchase of the winery. [77]

The Court: Negotiations with you or with Weller?

The Witness: With me.

Q. (By Mr. Koster): And the stipulation shows that the sale was concluded and Garrett and Company was released from the lease of 1944?

A. Right. That's right.

Q. Was there a demand for The DeTurk wines in 1942 and 1943?

A. Oh, yes, our wines always have a good reputation and it was in demand all over. We had inquiries from all over the country for it.

Q. Mr. Grace, do you have any opinion as to the value of the good will or the going concern value of the DeTurk Winery business conducted by Grace Bros., Inc., the value of those assets, in January, 1943?

A. Well, the value of the winery for seven years previously had made for us about \$20,000 each year. One year it made over \$30,000. Then with the other activities that we had there—if we had been able to give more attention to the winery, we could have made \$30,000 a year. One year we made it and the other seven years prior to the sale we averaged a little bit less than \$20,000 for the year for the seven years.

Based on that approximately \$20,000, I figured that it was worth five times that earning power.

(Testimony of Joseph T. Grace.)

The Court: Annual earning power?

The Witness: Annual earning power.

Q. (By Mr. Koster): Do I understand you correctly? What was it that was worth five times the earning power?

A. Well, I figured the good will. First there was the—we turned over to Garrett and Company our permit to manufacture wine and our license to sell it. We turned all of our rights over.

Then I consider that the reputation of the wine that The DeTurk Winery had—I think then it was valuable to have the wine identified under the De-Turk label. Our organization was valuable. The place in which to [78] do business was well equipped and valuable.

Q. Would you state what, in your opinion, was the value of the intangible or good will value of The DeTurk Winery business in January 1943 in amount of money?

A. I would say \$100,000, five times the earning power, which would be \$100,000.

Q. Would you say there was any difference in that value if you were to use as the valuation date June 1942?

A. No. I think the values would be about the same. The conditions improved though about that time. They were getting better, but they would result in very little difference, I think.

Q. Just one more question: This DeTurk Winery business was always located in Santa Rosa and conducted from there, is that correct?

(Testimony of Joseph T. Grace.)

A. That's right.

Mr. Koster: That concludes the direct examination.

The Witness: In connection with that other good will, I think the list of our customers and the capacity to make money there entered into my idea as to what went to make up the value of the good will in addition to the reputation of the wine. The company was making \$20,000 a year and the good organization we had, that we had trained for many years, all of that I felt was very valuable as well as the opportunity for them to go on and make their \$20,000 a year.

We had a distillery there; we were making very fine brandy.

Mr. Koster: Has the company at any time since then gone back into the business of making and selling wines?

The Witness: No.

Mr. Koster: Have you personally gone into that business?

The Witness: Of selling wines? No. [79]

Cross Examination

Upon cross examination by Mr. McFarland, Mr. Grace testified as follows:

Q. (By Mr. McFarland): Mr. Grace, you sold that winery plant in 1944 to Taylor and Company for \$150,000, didn't you? A. That's right.

Q. And the cost of that winery was \$50,997.36. Is that the way you computed the gain?

A. That was the depreciated cost.

(Testimony of Joseph T. Grace.)

Q. That was the adjusted cost at the time you sold and you realized a gain of \$99,002.64?

A. I think that is correct. As to that, I haven't the figures with me, but I think that is correct.

Q. That is the way you reported it for income tax purposes.

There is no element of good will in that, would there be? A. In the sale of the winery?

Q. Yes. A. In the sale of the winery building?

Q. Yes.

A. I considered there would be because it was an established winery and a place to do business, but I figured the good will to more on the wine inventory and the buying and selling of the wine than I did on the building.

Q. Well you said you valued the good will at January 1, 1943 at \$100,000.

A. That's right.

Q. Is that in addition to this good will that you propose to find out? [80]

A. No, that would take in all of it I figured.

Q. That would take in the whole thing?

A. That is the way I figured the winery and the wine business, the buying and making of wine, that it should reasonably be worth \$100,000.

Q. For the whole thing?

A. For the whole thing, that's right.

Q. Now you speak of turning over some permits to manufacture some wine. That permit applies to manufacturing wine at the particular winery, is that right? A. That's right.

(Testimony of Joseph T. Grace.)

Q. And whenever anyone in the State of California at least turns over and transfers by sale or otherwise a winery, the permit dies and a new one has to be taken out by the new operator?

A. Well, that is true, but the new operator can't get a permit unless the other fellow gets out of his way and surrenders his rights. We had to surrender our rights before Garrett and Company could get a permit to do business.

Q. What rights did you surrender?

A. We were operating the business and that was one—we had the possession of it and we were operating and Garrett and Company couldn't do business there until we got out of it.

Q. In other words, you surrendered the possession in order to let them get in there to make some wine?

A. That is true, but they couldn't until we turned over our rights to the permit.

Q. Your rights to the permit? How long were your permits in effect when you turned over the rights to make wine in that plant? [81]

A. Well, if the deal had not gone through, we would still have had the permit to make wine, to manufacture wine there.

Q. Surely, but in event the deal went through?

A. That was part of the transaction. When we made the deal with Garrett, we would turn over our permit, make it possible for him to get the permit to make wine.

(Testimony of Joseph T. Grace.)

Q. Presumably Garrett and Company would not have any interest in the lease of the winery unless they could make some wine in there, would they?

A. That is true, that is true; but they couldn't get the permit until we turned our rights over, which we had there.

In 1943 I was President and director of Joseph T. Grace Farms, Inc. I was the majority stockholder. The Farms Co. grew very few grapes. Grace Bros., Inc. grew the grapes. The products of the Farms Co. were mostly hops and grain but not any grapes. Grace Bros., Inc. grew some grapes in 1942 and I think they grew some grapes in 1943 and 1944. They have grown grapes for a number of years. I don't recall now when they first started growing grapes but it was several years previous to 1942, at least as early as 1940 and maybe a few years earlier. They have grown grapes since 1940 and each year thereafter. We made the grapes into wine when we operated the winery and sold them to Garrett and Co. after they took over. Now we sell the grapes to different wineries.

Q. Now we will take the Grace Bros. Brewing Company of Los Angeles. What is the connection as to the ownership of stock between that company and the Petitioner? Any connection?

A. Not at the present time. [82]

Q. In 1943? All my questions are asked in connection with that year.

A. In 1943. I don't think there was any Grace Bros., Inc., ownership there in 1943.

(Testimony of Joseph T. Grace.)

Q. Did you own stock?

A. Wait a minute—I wouldn't be so sure of that. We have several companies. I wouldn't be sure about that. Yes, I think Grace Bros., Inc., in 1943 and since owned stock in the Grace Bros. Brewery, Ltd., in Los Angeles.

Q. You have always owned stock in that company, haven't you?

A. Up to a great many years.

Q. I am talking about you personally.

A. Personally I sold some stock. I did for a while. I think the Grace Bros., Inc. at the present time owns most of the stock of Grace Bros. Brewery Ltd., in Los Angeles.

Q. Directing your attention to January of 1943 and December of 1942, what is the fact as to your own personal stock ownership of Grace Bros. Brewery, Ltd. at Los Angeles?

A. In—you mean at the present time?

Q. During December of 1942 and January of 1943.

A. I think in 1943 Grace Bros. Brewery, Ltd., owned practically all of the stock in the Grace Bros. Brewery, Ltd.

Q. Grace Bros. Inc., owned?

A. That's right. Owned practically all of the stock of the Grace Bros. Brewery, Ltd., in Los Angeles.

In 1942 I think I owned about two-thirds of that stock individually.

Q. Now the Buffalo Brewing Company—what is

(Testimony of Joseph T. Grace.)

the fact as to that company in 1942 and 1943—as to stock ownership in it? [83]

A. Well, that stock is owned—I am the largest stockholder there. My daughter owns some of that and I think, well, Mrs. Grace might have a small lot of it, but my daughter and I own most of it and I own most of the Buffalo stock.

Q. Do you or does Grace Bros., Inc., operate a Fresno Brewing Company?

A. Grace Bros., Inc.

Q. It operated that in 1942 and 1943?

A. Not in '42. It was purchased by Grace Bros. Brewing Company in 1942 and Grace Bros. has operated it since then.

Q. Is it a fact that in all of these other companies that counsel inquired of you, on your direct examination, that you or Grace Bros., Inc., own the majority or all of the stock in them and did in 1942 and 1943 for all practical purposes? I don't expect you to remember each exact share.

A. I don't remember each one of them. It's a difficult thing. I have a lot to attend to, but I owned most of the stock. Grace Bros., Inc., owned, I think, all of the stock in the Los Angeles Brewery. I think that I own a part of the Buffalo stock with my daughter. That is my recollection. The Fresno Brewing Company is owned by Grace Bros., Inc.

The California Ice Co. is owned jointly by myself and my daughter. I am a director of Bay Cities but I don't own any stock. That is owned by my

(Testimony of Joseph T. Grace.)

daughter and her children. Santa Rosa Ice and Cold Storage Co. is owned by Grace Bros., Inc.

Q. (By Mr. McFarland): You were active and you performed duties regularly—maybe not daily but certainly at periodic intervals, in all of these companies? A. Yes, sir. Too much so.

Q. That kept you pretty busy? [84]

A. That is the reason I got out of the wine business.

Q. You knew you had to get out of something?

A. I knew I had too much work to do.

Q. I believe as to actual facts as to the way the sale of the wine worked, there was a certain payment made by Garrett and Company to Grace Bros. in 1942, wasn't that right?

A. I think that's right.

Q. Grace Bros. Inc., filed an income tax return in 1942, didn't they? A. I think so.

Q. Do you recollect how and in what manner that payment was treated, as to whether it was treated as just the sale of wine?

A. I don't recall just what that is. That is a long time ago and with all these companies I have told you of, I can't remember. The income tax man is in the Court. He could tell you. I don't follow those things myself.

Q. You wouldn't know if I referred you to the returns? A. I would not, sir.

Q. Who is that gentleman?

A. The gentleman sitting in the corner.

(Testimony of Joseph T. Grace.)

Q. He would know how he accounted for the proceeds of the sale?

A. I think he would. I don't know myself.

Q. Does Grace Bros. Inc., hold regularly scheduled meetings of the Board of Directors?

A. Well, we hold meetings occasionally.

Q. None of these considerations that you have testified to as to the desire to dispose of your winery ever reached written form in the nature of minutes, did they? [85]

A. I don't recall, sir, about that. I know it was the general decision that we should get out of the wine business.

Q. Who makes that decision?

A. I am largely responsible for those decisions. These different companies and things—we have been engaged in business up there for many years, for 50 years nearly, and these companies have grown up and largely around through our own efforts. The decisions on these things largely rested with me, though.

Q. Who comprised the Board of Directors of Grace Bros., Inc., in 1942?

A. I think Mrs. Grace and Mr. Kadan and myself.

Q. Did Mrs. Grace own stock in Grace Bros., Inc., at that time? A. I think she did.

Q. How many shares of stock did she own?

A. Well, Mrs. Grace had at least the qualifying number of shares, but she had some other stock she was going to buy, quite a substantial amount of it,

(Testimony of Joseph T. Grace.)

but for some reason or other Mrs. Grace didn't want to conclude the purchase. So the stock was undelivered and I still own most of the stock in Grace Bros., Inc.

Q. How many shares are authorized to be issued? A. I think a thousand.

Q. How many have been issued?

A. I think a thousand; originally there were 2,000 and on the death of my brother in 1930 the stock issue was reduced from 2,000 shares to 1,000 shares.

Q. How many shares did you hold in 1942, during 1942?

A. I held practically all of it outside of what arrangement Mrs. Grace was going to buy and then Mrs. Grace didn't conclude. She changed her mind about what she wanted to buy. [86]

Q. The deal fell through?

A. The deal fell through. I still own the stock.

Q. Did Mr. Kadan hold a qualifying number of shares? A. That's right.

Q. He never held more than that at any time?

A. No.

Q. You own 99 percent of the stock?

A. I think so.

Q. You ran the company?

A. That is correct.

Q. You might have told them on certain decisions, what the facts were, and maybe you didn't, too?

A. No. We discussed things pretty well back

(Testimony of Joseph T. Grace.)

and forth on that. But we have been operating together for a good many years and we're still getting along all right.

Thereupon the following telegrams were offered and received in evidence as respondent's Exhibit I.

First telegram, dated December 28, 1942, to Joseph T. Grace at Santa Rosa, California from Garrett and Co., Inc.

Second telegram, dated December 28, 1942, addressed to Garrett and Co., Brooklyn, N. Y. from Mr. Grace.

Third telegram, dated December 28, 1942, addressed to Garrett and Co., Inc. at Brooklyn, signed by Joseph T. Grace.

Fourth telegram, dated December 29, 1942, addressed to Joseph T. Grace, Santa Rosa, California from Garrett and Co.

Fifth telegram, dated December 29, 1942, addressed to Garrett and Co. at Brooklyn, N. Y. from Joseph T. Grace. [87]

Sixth telegram, dated December 30, 1942, addressed to Joseph T. Grace from Garrett and Co., Inc.

Seventh telegram, dated December 31, 1942, addressed to Joseph T. Grace from Garrett and Co., Inc.

Eighth telegram, dated January 1, 1943, addressed to Garrett and Co. by Joseph T. Grace.

Ninth telegram, dated January 2, 1943, addressed to Joseph T. Grace from Garrett and Co.

(Testimony of Joseph T. Grace.)

Q. (By Mr. McFarland): Mr. Grace, these telegrams are arranged to the best of my ability in chronological order. A. Yes.

Q. Let us take up the telegram of December 28, 1942. Would you read that?

The Court: Is that the first of the series?

Mr. McFarland: That is the first of the series.

A. It was a telegram from New York to me:

“Roy Weller is here and hears you are interested in selling your inventory and leasing winery for a term of years. If so, please give us details. Would also appreciate it if you will hold matter open until we can consider it.”

Q. (By Mr. McFarland): The next telegram is dated December 28, 1942. Would you read that telegram?

A. “Telegram received. Please advise Roy Weller that we have several purchasers—”

Q. Pardon me. That telegram was sent by you, is that correct?

A. That's right. It is the one I am going to read now. [88]

Q. Yes.

A. “Telegram received. Please advise Roy Weller that we have several purchasers for our inventory and lease of winery and distillery. Also bonded warehouse. Stop. Inventory consists: Dry red mostly from Zinfandel and Petitsyrah 1940 vintage 180,000 gallons, 1937 vintage 5,000, 1939 vintage, 5,000, same kind black grapes. Price for all forty

(Testimony of Joseph T. Grace.)

cents per gallon. Stop. About 80,000 gallons dry white wine practically all from Northern white grapes made up as follows: About 15,000 gallons 1937 vintage, sixty five cents per gallon. About 260,000 gallons sweet wine made up of port, about 40,000 gallons vintage 1935-1941. Muscat, about 120,000 gallons all from 1935 and 1938 vintage. Sherry about 70,000 gallons 1935 and 1938 vintage. About 20,000 gallons Angelica 1938, 1939 and 1941 vintage. Sixty five cents for all sweets. Stop. Lease of winery, distillery and bonded warehouse \$12,000 per year for five years. Stop. Please telegraph by Western Union Tuesday morning early if you are interested. Stop. Would prefer doing business with your company if possible as other prospective purchasers are strangers but have good financial recommendation. This is not an offer to sell to you, only an indication of position. Happy New Year."

Now, may I remark something about this telegram, sir?

Q. Probably we would expedite the matter, Mr. Grace, by not doing so, because I know Mr. Koster will undoubtedly ask you questions.

A. All right. All right.

The next one is to Garrett and Company signed by me:

"Can probably add 100,000 gallons port and 100,000 gallons muscat both 1940 vintage to inventory in my telegram today at 60 cents. Answer immedi-

(Testimony of Joseph T. Grace.)

ately by Western Union if interested. Can sell to other parties." [89]

The next telegram, December 29, 1942:

"Situation with reference transportation which has arisen since our wire of yesterday makes us hesitate take on wine listed in your wire. However we might be interested in portion of inventory if you cared to dispose of part. Thanks for wire and best wishes for new year."

Next wire, to Garrett and Co., sent by me:

"Your wire recd. What part of inventory are you interested in. Stop. What are your ideas on rental of plant. Stop. Anxious to close deal immediately to get part of sales in this year income tax returns. Answer by WU care St. Francis Hotel."

December 30, a wire from Garrett and Co.:

"Weller and Moore out of city returning tomorrow and will then wire definitely regarding inventory and rental of plant."

Q. That is signed by Garrett and Company?

A. That is signed by Garrett and Company.

The next, dated December 31, 1942, signed by Garrett and Company:

"Confirming our telephone agreement relative to lease of winery and purchase of bulk wines as follows . . ."

There have been many telephones in between these and I feel that would change the complexion of these telegrams a lot.

Q. Will you read that?

A. Yes.

(Testimony of Joseph T. Grace.)

“ . . . We lease your winery located at Santa Rosa, California as of January First 1943 for a period of five years with an option on our part for a five year renewal at an annual rental of ten thousand dollars. We purchase approximately 520,000 gallons of bulk wine as set forth in your telegram of December 28th at an average unit price of fifty cents [90] per gallon naked FOB Santa Rosa, California, if found to conform to California State Standards. A deposit of 20% of purchase price of wine to be paid you at once and held by you to apply as payment for final shipments. Individual payments to be made on each car of wine as shipped until deposit can be applied. Further understood that entire agreement as outlined above is subject to immediate cancellation as to lease or purchase of any wine remaining unshipped in event tank cars cannot be secured for movement to Brooklyn, New York.”

That wasn't agreed to. That was stricken out.

Q. That is in addition, Mr. Grace. We're getting ahead of ourselves. It is in the telegram.

A. Yes, it was in the deal, but after it was taken out.

“Other necessary details and final signing of agreement will be completed upon arrival of L A Weller in California about January 20.”

January 1, telegram from me:

“Accept your proposition in telegram dated December 31st. My understanding from phone con-

(Testimony of Joseph T. Grace.)

versation was that you would start shipments of wines in the near future and that you would move all of same in a reasonable time. Stop. We have several hundred wine barrels which other wineries have made proposition to purchase. Do you think it advisable to hold these barrels for your possible Eastern shipments in event tank cars become scarce. Stop. Have billed you for a portion of the inventory to get same in last years business for income tax purposes. Stop. If convenient please mail check for deposit as mentioned your telegram December thirty-first. Wine inventory and winery's property are free of all debt. Stop. Note your Mr. Weller will arrive California about January twentieth [91] to sign wine agreement and lease. Stop. Rest assured that I will do everything possible to assist your organization in making success of your program here. Stop. Happy New Year."

Signed by Joseph T. Grace.

Then the telegram dated January second from Garrett and Company, Incorporated, to me:

"Mailing you check today for fifty-two thousand dollars covering initial deposit. Please hold wine barrels as possibility we might need them. Weller will discuss with you upon arrival. Our intention move wine East as fast as tank cars can be secured for movement."

Q. Now, Mr. Grace, referring for the moment to your direct testimony, I believe that you stated that you desired to get out of the winery business in 1942, is that right? A. That's right.

(Testimony of Joseph T. Grace.)

Q. What influenced you other than what you have already testified to, namely, your preoccupation with other activities in which you or Grace Bros., Inc., were busily engaged? What influenced you to arrive at this decision?

A. Oh, I think it was likely a little too much work and too much activity.

Q. There was a shortage of tank cars in 1942?

A. They were becoming scarce. It never developed into a shortage.

Q. At that time, everybody was apprehensive about the situation?

A. Not particularly so. I told Weller after this telegram here which refers to the tank car shortage that we wouldn't make a deal with him on that basis and he said, "Well, take that out." This he did. He wasn't very apprehensive about it. [92]

Q. The price of wine was going up those years, wasn't it?

A. Well, it was improving. There was a better feeling for it.

Q. Did the OPA price ceilings or any restrictions on it have anything to do with the difficulty of conducting business that would make it desirable for somebody managing it to go out of business, forget the whole thing?

A. No, I don't think so. I don't think we ever had any difficulty on that.

Q. How many key men did you consider that you had in 1942 in your organization?

(Testimony of Joseph T. Grace.)

A. Well, let me see. There was one—Oh, I'd say three or four key men.

Q. How many men did you have in the organization—I am not talking about the season.

A. Not in the crushing season—in the ordinary work I would say about eight, maybe ten, and during the vintage when we were crushing grapes, we would have maybe three times, two or three times that.

Q. Mr. Grace, in arriving at your valuation of your intangible or good will inherent in this sales price, you stated that you roughly estimated five times the average earnings over a period of years as being representative of that figure, is that correct?

A. That is correct.

Q. Why did you adopt that formula or how did you come to use that formula?

A. Well, in my banking experience, why the earnings of a business per year—we have used that formula at different times. [93]

Q. You have used that formula in evaluating a credit risk in your bank?

A. Yes. The average earnings of a business annually has to do with the value of it. That is the way I have always figured it.

Q. And you have drawn upon your experience as an advisor to the Santa Rosa Bank of America Branch, is that right?

A. Well, my experience when I was in charge of the banks up there and since then, yes.

(Testimony of Joseph T. Grace.)

Q. Your experience consisted mainly of evaluating, determining whether or not this particular applicant would be a good risk or the corporation in large part, at least?

A. Well, of course the business had to have the earning power in order to repay the loan. That always entered into it.

Q. That was one of the factors?

A. That was one of the factors.

Q. And the other facts would be the normal factor in determining whether it was a good risk or not, is that right?

A. The other factors would involve the reputation of the men in charge of the business and their qualifications for operating the particular business in which they were engaged.

Q. But my point is you were approaching the problem at that time from the Bank viewpoint in determining whether or not to extend credit to a particular applicant.

A. That is the way I would figure. That is the way I would ascertain it. Good will value or the earning value would be as to what the business was making each year, the annual earnings. [94]

Q. Now will you answer my question?

When you were with the Bank of America, busy with that particular problem, namely, determining whether or not a particular applicant was an acceptable credit risk, you took into consideration various factors that anyone would in determining upon the credit risk?

(Testimony of Joseph T. Grace.)

A. Yes. But I had other duties in addition to that to perform. That was not my only duty.

Q. That was your main duty?

A. No. I wouldn't say it was the main duty. I had other duties that I consider equally as important.

Q. What else did you do?

A. I had supervision of the branches, the help, and—

Q. When you say "supervision" over the personnel, what do you mean? A. I had charge of—

Q. The personnel, is that it?

A. Yes. I consider I was in charge of the personnel.

Q. Yes.

It is my understanding by the way Mr. Weller, whom we have referred to and who is an official of Garrett and Company, is now deceased?

A. I understand so.

Q. Yes.

What is your recollection as to the average capital investment of Grace Bros., Inc., over the years 1936 to 1942?

A. You mean in all of the businesses?

Q. Yes.

A. In all of our different lines? [95]

Q. In this particular business.

A. In the wine business?

Q. Yes.

A. I think the winery showed after depreciation about \$60,000 and I think the investment in the wine

(Testimony of Joseph T. Grace.)

inventory, after depreciation and cost, figured somewhere around \$90,000, if I am correct.

Q. Yes.

In connection with this decision that you claim to have made in the early part of 1942 relative to your winery and your wine business, did any of it ever find expression on any written document or any paper that you know of, belonging to the Company, in the form of a resolution or a minute or communication or a memorandum?

A. I don't recall as to whether or not our minutes show anything on that or not.

Q. You have checked your minutes recently, haven't you? A. No, I haven't.

Mr. McFarland: Do you have the Minute Book here, Mr. Koster?

Mr. Koster: Government counsel and I examined the Minute Book and there is nothing concerning this in it.

Q. (By Mr. McFarland): There would be no other place where a memorandum would be available that would shed any light on this?

A. No. I don't think so, Mr. McFarland.

Q. None of this ever reached paper?

A. That is a decision to go out of the wine business?

Q. Or any of the considerations or discussions that you had with anyone or your ideas or your reasons—none of it ever reached paper?

A. I don't think so. I was the Executive officer

(Testimony of Joseph T. Grace.)

and largely made those plans myself. But I don't know of them ever reaching paper. [96]

Q. You wrote the memorandum of agreement and lease that you composed in the form of a letter to Garrett and Company, did you not?

A. I don't think I did. I don't recall of doing so.

Q. This is a photostatic copy. It is attached to the stipulation of facts.

A. Well, it was not prepared by me. It might have been prepared by our attorney. I am sure I didn't prepare it.

Q. You signed it. You signed the original. You read it over, didn't you?

A. No—well, I must have before I signed it. I haven't read it recently.

Q. What is said in there certainly at the time you read it over and signed it was true or in accordance with your decisions in the matter, in accordance with your ideas?

A. Well, I presume it must have been or I wouldn't have signed it.

Q. Surely. That is all I was asking, Mr. Grace.

Redirect Examination

Upon redirect examination by Mr. Koster, Mr. Grace testified as follows:

I don't know the date of Mr. Weller's death but I think it was about a year ago. That is as close as I can figure.

Q. (By Mr. Koster): Mr. Grace, I am showing you Defendant's Exhibit I which is a group of telegrams, and I call your attention to the first tele-

(Testimony of Joseph T. Grace.)

gram which is addressed to you by Garrett and Company, Inc., and it is dated December 28, 1942. I ask you whether or not your conferences with Mr. Weller in Fresno, to which you have testified to on direct examination, occurred prior to that date? [97]

A. Yes, they did. The conference was prior to this date of December 28.

Q. Did you consider that this telegram related to that conference?

A. Well, when I talked with Mr. Weller there, he indicated that Garrett and Company might be interested in leasing the winery and in paying the price to us for the wine that would meet the price we asked for the wine business. Then when I received this, he said he would see his people when he went East, and then this telegram was construed by me to be that they were interested in the deal because it was some time prior to this time that we held that conversation.

Q. I call your attention, Mr. Grace, to the second telegram which is sent by you, addressed to Garrett and Company, Inc., and I ask you if there was any particular reason for the context of that telegram in the manner in which it was composed?

Mr. McFarland: Is this the telegram dated December 28th, Mr. Koster?

Mr. Koster: December 29, it appears. Well, I suppose it was sent on the 28th. It was a Night Letter and seems to be a December 29 date on it

(Testimony of Joseph T. Grace.)

also. It is the second telegram in the group of telegrams made a part of that exhibit.

A. Well, this telegram was simply a listing of the wines, of the wine inventory that we had for sale. These prices that I asked Garrett and Company, they would have given us a little bit more for the wine and the good will than what we eventually received. It was just a listing of the wines, and I asked him—I thought that Garrett might pay these prices on account of the interest evidenced in previous meetings. If he had, I of course would have received a little more on these prices than eventually on the wine and good will, than we eventually received. [98]

The Court: Those prices fluctuated with reference to different types of wine, whereas your talk with him was a flat price on all wines?

The Witness: Well, the flat price for the wine originally—I told him we wanted \$250,000 for the wine inventory and the good will. Then there was some request made for an inventory or a listing of the winery, the wine stock, and these prices, Your Honor, would have figured a little bit more than \$250,000.

The Court: I understood yesterday that you figured you got about 50 cents and that probably was a little bit more. Most of that is above 50 cents.

The Witness: This would be above 50 cents; this would give us more than 50 cents by a little bit more than \$30,000.

Q. (By Mr. Koster): Was this in line with your

(Testimony of Joseph T. Grace.)

conversation with Mr. Weller at the conference in Fresno to which you testified?

A. Well, these prices are a little higher and it is the same wine though that we offered to sell him. But I asked him at first—I indicated that we wanted \$250,000 for the stock and the wine and the good will and this that we have presented and itemized would have figured up a little more than \$250,000.

Q. I see.

The Court: Pardon me. Where is the headquarters of this company that is buying the wine? Is that in New York?

Mr. McFarland: Brooklyn, New York.

The Witness: And they have a place in Cucamonga, in Southern California.

Q. (By Mr. Koster): I call your attention to the wire dated December 29, 1942, a day letter signed by Garrett and Company, and addressed [99] to you, in which reference is made to possible shortage of transportation and a request of you whether you would be interested in selling a portion of your inventory. I also call your attention to your reply to that wire by wire dated the same day, December 29, in which you make an inquiry of them of what part of the inventory they might be interested in and that you would like to have the matter closed so you could have it in your income tax returns for 1942.

Was there any reply received to your answer, or was there any further steps towards developing the matter of selling the inventory in part?

(Testimony of Joseph T. Grace.)

A. I told him that we would not sell a part of the inventory.

Q. When did you tell them that?

A. Well, I think that must have been about the time or the day, either the day or the day after, that we received the wire, that we would not be interested.

The Court: Is there a telegram to that effect?

Mr. Koster: I will follow that up, Your Honor.

Q. (By Mr. Koster): Now I call your attention to the final wire or the next to the last wire, dated December 31, 1942, addressed to you by Garrett and Company. I notice that wire starts off with the words, "Confirming our telephone agreement * * *" Is that the telephone call in which you discussed the matter of selling partial inventory?

A. Yes. I am quite sure it is because it was the following day and I told them in that telegram we would not be selling—

Q. Telephone call?

A. Telephone call, that we would not be interested in selling a part of the inventory. They indicated that they would consider that, and then [100] later on they agreed to take all the wine. They sent us a telegram they would ship all of the wine, as I recall.

Q. Now before we get to that, and calling your attention again to this wire of December 31 which I wish you would read—and I call your attention especially to a provision in that telegram concerning possible cancellation.

(Testimony of Joseph T. Grace.)

A. I told them on the phone that we would not agree to any cancellation of part of the deal. The deal was that they would have to buy it all or nothing and that there would be no cancellation clause considered.

Q. And what did they say to that?

A. They answered, then, I think, either the same day or the day after, that they would ship all of the wine, which they did.

Q. Did you confirm this agreement or the agreement that was made over the telephone?

A. I did.

Q. And now I call your attention to the wire dated January 1, signed by you, and addressed to Garrett and Company, Inc., in which it is stated "Accept your proposition in telegram dated December 31st. My understanding from phone conversation was that you would start shipments of wines in the near future and that you would move all of same in a reasonable time Stop."

Is the telephone call referred to in that telegram the telephone call to which you have just testified concerning the removal of all cancellation provisions? A. That's right.

Mr. Koster: Your Honor, I omitted to ask one question on direct examination and I would like to just ask this question, if you please. [101]

Q. (By Mr. Koster): Mr. Grace, there is attached to the stipulation of facts in this proceeding as Exhibit 4-D a statement of the earnings of the DeTurk Winery for the years 1936 to 1942 inclu-

(Testimony of Joseph T. Grace.)

sive. I note from that statement that the income for the years '39, '40 and '41 was lower than in any of the other years.

I ask you whether there is any particular reason why the income in those years was lower than in the other years?

A. Well, the wine business in those years was not as good as in the previous years or in the later—well, the previous years. It was those years where the prices were down and a little bit lower, maybe, and the wine trade was quiet.

Mr. Koster: That is all.

Recross Examination

Upon recross examination by Mr. McFarland, Mr. Grace testified as follows:

Q. (By Mr. McFarland): Mr. Grace, I would like you to take your telegram that you sent to Garrett and Company, dated December 28, and your telegram, your second telegram, dated December 28, and compute for me on the basis of the prices that you have mentioned of the various wines that were in the inventory, your formula for five times the earnings of the business. I would like to see how you work it, either way.

A. Well, let me see. I don't understand your question.

Q. You have enumerated various prices for different kinds of wine in your inventory in those two telegrams.

A. That's right.

Q. Now I want you to compute for me on the basis of those telegrams the value of the good will

(Testimony of Joseph T. Grace.)

and the intangibles that you claim were sold to Garrett and Company on the basis of those telegrams.

A. I don't see where these telegrams would have any connection.

Q. I am just asking you the question. Can you do it?

A. Well, I think I testified that my computation—

Mr. McFarland: I think the answer should be responsive to the question or he should state that he can't do it.

The Court: The witness will answer the question as he understands the question, as he knows the answer to be correct, whatever it might be.

Repeat the question and let him answer it, Mr. McFarland.

Q. (By Mr. McFarland): I would like you to compute for me the intangible value that you claim was transferred by the sale of this wine to Garrett and Company upon the basis of the prices that you have set forth relative to the various types of wine that were in your inventory at the time you sold that inventory to Garrett and Company.

A. Well, I computed the good will value on the basis of the business the winery had been doing for five years, for seven years.

Q. Mr. Grace, can you compute the good will value on the basis of those telegrams?

A. On the basis—the good will value on this particular transaction (is that correct?) that would be most difficult to do. It is only a portion of a year;

(Testimony of Joseph T. Grace.)

it is only a part of the time. The good will value—

Q. I am just asking you, Mr. Grace, if you can compute the good will on the basis of the prices mentioned in those telegrams.

Mr. McFarland: If the Court please, that doesn't appear to be a difficult question.

The Court: He answers according to the way he understands it. [103]

A. I computed the good will value of the winery business thereon the profits that the winery business had made for the seven preceding years, which was approximately \$20,000 a year.

Q. (By Mr. McFarland): Then if I understand you first, Mr. Grace, you can't compute it on the basis that I ask?

A. I suppose as a mathematical proposition it could be done in some way, but it would require a lot of time.

Q. You didn't do it in that way?

A. No. I computed it, the good will value, on the profit that the winery business had made for seven preceding years.

Q. Then am I correct in stating that you determined the prices that you would sell the various types of wine at with the idea in mind of having the prices average roughly 50 cents per gallon. Is that right?

A. These prices that you speak of, Mr. McFarland, I think would give us about \$30,000 more than 50 cents per gallon.

(Testimony of Joseph T. Grace.)

Q. But that was roughly what you were shooting at?

A. I asked Mr. Weller for the \$250,000 which included the good will, and I figured that I could get out of the wines as we were selling them, about \$150,000, and I asked \$250,000 because I figured that the good will value in there was worth \$100,000 and that was five times the approximate earnings of the previous year.

Q. And you got the \$100,000 on the sale of the plant subsequently, did you not? You realized a hundred thousand dollars on the sale of your winery?

A. I don't know just how that would figure out.

Q. We went over that yesterday, don't you recollect, Mr. Grace? [104]

A. That would be only a part. The profit off the winery would only be a part because there was the organization, and a lot of other attributes in there, but as to just what we made on the winery sales, I don't know what the computation would show.

Q. You made \$99,002.64 on the winery sales?

A. That might be, and I don't know that and I didn't figure that in the \$100,000 that I figured the good will. That would only be a part. The profit we made on the wine would be only a part because I figured in that valuation for the good will of \$100,000, I figured the reputation of the wines, the wines under The DeTurk label and the organization, these men that we had trained for years to make this wine. I figured our customer list, the people to

(Testimony of Joseph T. Grace.)

whom we sold the wine. I figured the capacity of this business to make money. That is what I figured for the \$100,000.

Now what we made a year or so later on the sale of the wine I have never checked into that.

Q. You wouldn't say this is incorrect?

A. I wouldn't say it is incorrect. It might be correct, but I have never checked in to see the depreciated value of the winery.

Q. As a matter of fact, Mr. Grace, you have stipulated that this is correct. Your counsel has stipulated.

A. If we have, it must be correct.

Q. Will we agree it is correct?

A. I can't agree to that. I don't know, but if it is stipulated, it must have been our income tax man who furnished these figures. But I haven't my personal knowledge it is correct.

Q. Tell me why did you sell the plant for \$150,000?

A. Well, I thought we could get it. [105]

Q. How did you arrive at that figure?

A. How did I arrive at that figure? I think there might have been some other wineries sold or I think this man came along, I forget just how this thing came up, but we asked \$150,000 and he said he would pay it.

I might have taken a little less, but he paid the price I asked.

Q. And you had the depreciated cost in that winery of \$50,000 roughly?

(Testimony of Joseph T. Grace.)

A. I don't know. That might be correct, sir, but I don't know.

Q. No other considerations other than what the fellow said he would pay?

A. He wanted the winery and he asked me what I would take for it or what we would sell it for and I told him \$150,000.

Q. How did you compute that figure?

A. I thought that was worth that. I thought we could get it and like anything you have to sell, you will sometimes ask a pretty good price.

Q. And take less, is that right?

A. Well, maybe take less. That is true.

Q. You didn't compute mathematically or take anything into consideration other than just what you thought he would pay?

A. That is about it.

Q. Garrett and Company never put out wine under The DeTurk label, did they?

A. I don't know.

Mr. McFarland: I believe that is all.

Further Redirect Examination

Upon further redirect examination by Mr. Koster, Mr. Grace testified as follows: [106]

Q. (By Mr. Koster): You testified to direct examination that when you met Mr. Weller in Fresno you asked a price of \$375,000 for the business, which included \$125,000 for the winery and \$250,000 for the inventory and the business. Is that correct understanding?

A. Yes, that is correct. \$125,000 for the winery

(Testimony of Joseph T. Grace.)

and \$250,000 for the wine inventory and the good will, making \$375,000.

Mr. Koster: That is all.

There being no further questions the witness was excused.

Thereupon,

JESSE TAPP

was called as a witness for and on behalf of the petitioner and first having been sworn was examined and testified as follows:

Direct Examination

By Mr. Koster:

My name is J. W. Tapp. My business address is 300 Montgomery Street. My home address is Palo Alto. I am employed by Bank of America as Vice-President and a member of the General Finance Committee. At the present time that Bank is the largest in the United States. I was first employed by the Bank in 1939. In April 1943 I took leave of absence and was for three months associated with the War Food Administrator and then from July 1943 until April 1945, President of Axton-Fisher Tobacco Co., Kentucky. In April 1945 I returned to the Bank in my present capacity. The Axton-Fisher Co. manufactures cigarettes. The company had approximately \$22,000,000 in total assets and was doing a gross business of about \$10,000,000 a year. I was actively working as an executive officer of that company during the period mentioned.

In my position with Bank of America my special

(Testimony of Jesse Tapp.)

field is in connection with loans to agriculture and to the processing industries such as canners, dried fruit packers, wineries, other agricultural processing industries, although as a member of the General Finance Committee I have to be interested in all the credits of the bank. In my position I have reviewed or passed upon many millions of dollars of loans. Most of the loans to wineries of California which we handle, which is a considerable portion of them, go over my desk and I have considerable responsibility in connection with those. In addition, because of my previous experience with the Department of Agriculture, I have worked rather closely with the grape producing groups and wineries and raisin packers, in connection with their various marketing problems. We have made very extensive loans to the grape producing industry, to the raisin packing industry, to the shippers and to the wineries, both in the form of open credits on wine, raisins, or other products. In 1939 through 1941 we had a very large loan in connection with the RFC and some of the other banks to the wine industry as a whole, involving primarily California brandy. This brandy was made in connection with the diversion of surplus grapes to try to improve the situation in 1938, 1939 and 1940. In extending our credits, of course, we kept a rather complete financial file of all of our borrowers or those who had been borrowers and some who may be borrowers which we are quite familiar with and which

(Testimony of Jesse Tapp.)

we have to study as these credits come up from time to time.

Q. (By Mr. Koster): In making an analysis of credits and credit risks, did you at any time make any determination or give any consideration to the going concern value or intangible asset value of businesses engaged in the wine and grape industry?

A. Yes, in connection with a great many of them of going concern value, reputation, trade marks, and position in the trade, which is of value.

Q. Have you ever engaged in any business transaction in which you negotiated for the disposition of intangible or good will value of any business concern?

A. In connection with the Axton-Fisher Tobacco Company, that company was dissolved in 1944 and I had the responsibility of negotiating the sale of the plant and brands, trade marks, assets, physical assets, inventory, etc., to another concern.

Q. In the matter of analyzing risks for unsecured loans, have you at any time made any determination of value for the members of the grape and wine industry as to intangible or good will values?

A. Well, we have considered that. I wouldn't say we have made a determination, but in our consideration of the credits we naturally gave consideration to the ability of the company to sell its products and its ability to continue as a going concern, which might be in some cases of equal value

(Testimony of Jesse Tapp.)

to its physical assets or other financial factors that we would consider.

Q. Have you ever made any valuation or used any formula for determining any valuation for that type of assets?

A. Well, our—rather, I should say, the usual methods would be to try to arrive at some estimate of the company's earning power and capitalize that on some reasonable basis. We do that more particularly in connection with the valuation of farm property than we do with business property, although occasionally it comes up with business property.

Q. Have you ever testified in Court as an expert witness as to [109] determination of going concern value for any business concern?

A. I have testified in connection with valuation of farming property on the basis of its earning capacity.

Q. Have you, in making your analysis of intangible values, considered that those values are influenced by your determination of the extent of the reputation or value of the product or the earning capacity of any business concern?

A. Yes. That would be true. In the wine industry particularly the reputation of the wines and the location of the plant and general reputation of the management is important factor.

Q. Mr. Tapp, I show you a schedule which is marked Exhibit 4 D attached to the stipulation of facts introduced in this proceeding, which is a

(Testimony of Jesse Tapp.)

schedule of the earnings of the DeTurk Winery operations of Grace Bros., Inc., for the seven years 1936 to 1942 inclusive.

Assuming that the DeTurk Winery manufactured and sold wines of good reputation, assuming that they have been conducting business at the same location for all of these years and for years prior thereto, for as far back as 1921, assuming that they had a good organization and assuming that they sold their wine and operated their business under an identifiable trade name of The DeTurk Winery, which had a good reputation, I ask you whether you can give an opinion as to the going concern value of this company.

I also want you to assume that, as it has been stipulated in the stipulation of facts, this winery had an average investment in inventory and intangible property over this period of years of \$150,000 and I ask you whether with that information you can express an opinion as to the going concern value of The DeTurk Winery? [110]

Q. In expressing your opinion of value, I ask you to express it as of January, 1943.

A. Well, we have here aggregate net profits of approximately—

The Court: You are speaking of annual profits, average annual net profits?

The Witness: I am speaking first of the aggregate for the seven years, approximately \$133,000, which would be an average of slightly less than \$20,000.

(Testimony of Jesse Tapp.)

Now included in that period are the years 1939, '40 and '41, which were years of acute depression in the wine industry as reflected in very low earnings here and as reflected in what we know to have been very low earnings in the wine industry, in fact, losses for a great many members of the industry. Therefore I would raise some question as to whether or not the full seven year period would be adequate for determining normal average earnings that might be expected from a winery of this type.

If it included the years '43, '44 and '45 or a ten-year period, it would probably show a different average return.

The Court: Higher or lower?

The Witness: Higher.

If you take the four years exclusive of '39, '40 and '41, you would get an average of approximately \$25,000. So that, in getting an average net earnings for that purpose of capitalization, I would be inclined to take (having only the seven-year figures) those four years because those were not years of great profit in the wine industry and yet they were more representative of what you might expect for a considerable period of years than the period including these three low years. [111]

Capitalizing that, on the basis of eight per cent, you would get a going concern value, say, of \$300,000, a little over, \$310,000, as a going concern value of business earning that much over a considerable period of years.

(Testimony of Jesse Tapp.)

That would be my method of arriving at the going concern value of the entire business including the tangible and intangible assets as well as the other assets that the company has in the form of good will, reputation, etc.

Q. (By Mr. Koster): And if the tangible, if the investment of the tangible assets averaged as in this stipulation of facts, \$150,000 per year over a period of years, how would you arrive at the intangible value?

A. I would simply deduct the \$150,000 from the \$310,000 which would give you \$160,000 which was not represented by tangible assets.

Q. In making that computation you are assuming there would be the same rate of return on the tangible assets and on the intangible assets?

A. That's right.

Q. If you were to value the going concern value of this company in June of 1942, would you arrive at the same result?

A. Yes, because you are considering long-term earnings, and at the same rate of capitalization, I would get the same result.

Cross Examination

Upon cross examination by Mr. McFarland, Mr. Tapp testified as follows:

Q. (By Mr. McFarland): Mr. Tapp, in your computation, in your valuation, I should say, did you consider that the going concern value necessarily encompassed the sale of the trade name and

(Testimony of Jesse Tapp.)

labels of a winery and the right to manufacture wine under that trade name to the purchaser? [112]

A. I was assuming a sale of the assets responsible for it.

Q. Those items are assets that are responsible for producing income?

A. The entire income producing assets.

Q. Now the trade name and the right to manufacture wine under that label is certainly one of those assets, isn't it?

A. If there is a trade name and it has—

Q. Do you know whether or not there is a trade name here?

A. I am not familiar with the details of this winery.

Q. You are not familiar with the details of the sale at all?

A. No. I was testifying as to methods of computing the valuation.

Q. If a winery was sold and the wine inventory and the labels and the right to manufacture and all of the various concomitant parts were transferred, that is what you were considering, the basis of your consideration, is that right?

A. I was simply computing the going concern value based on the income producing demonstration of the property.

Q. Is the manufacture of wine under a certain label, that a winery has manufactured under that label for a number of years, that is certainly an asset you would consider in a transfer?

(Testimony of Jesse Tapp.)

A. That's right.

Q. And the right to manufacture the wine under that label by the new purchaser would be considered in your judgment, wouldn't it?

A. If that is a part of what is considered here in the net profits.

Q. I understand you didn't attempt to consider the various elements of the transaction at this particular occasion, is that right?

A. I am simply trying to tell you how we would convert net earnings into a valuation of the property. [113]

There being no further questions the witness was excused.

Thereupon, there was offered and received in evidence the following exhibits:

Respondent's Exhibit J, a photostatic copy of a letter addressed to Garrett and Company at Brooklyn, New York, dated March 29, 1943 by The De-Turk Winery by Manuel Felciano, attorney in fact;

Respondent's Exhibit K, a letter written under date of May 26, 1943 by L. A. Weller, addressed to Joseph T. Grace;

Respondent's Exhibit L, a letter dated June 18, 1943 from Garrett and Company by L. A. Weller to Joseph T. Grace;

Respondent's Exhibit M, an inter-office letter from Mr. L. A. Weller to J. Campbell Moore of Garrett and Company, dated November 5, 1946.

There being no further evidence the matter was submitted to the Tax Court.

The foregoing evidence and the Stipulation of Facts and Exhibits attached thereto and the Exhibits introduced in evidence at the trial, referred to herein and designated for inclusion in the record on appeal in the Designation of Contents of Record on Appeal filed concurrently herewith, is all the evidence adduced at the hearing before the Tax Court of the United States which is material to and necessary for the determination of the issues presented on appeal, and the same is approved by the undersigned attorneys for the petitioner on review.

/s/ GEORGE H. KOSTER,
/s/ BAYLEY KOHLMEIER,
Attorneys for Petitioner.

Agreed to: June 24, 1948.

/s/ CHARLES OLIPHANT,
Chief Counsel,
Bureau of Internal Revenue.

Margaret Goydich, being first duly sworn, deposes and says that she is a resident of the City and County of San Francisco, California, is over the age of 18 years and is not a party to the above cause and that she served the foregoing Statement of Evidence upon Charles Oliphant, Chief Counsel of the Bureau of Internal Revenue and counsel for respondent by mailing to him a true copy thereof in an envelope addressed to Charles Oliphant, Chief Counsel of the Bureau of Internal Revenue, Washington, D. C., bearing proper postage, and regis-

tered and deposited at the United States Post Office, Station D, San Francisco, California on June 15, 1948.

/s/ MARGARET GOYDICH.

Subscribed and sworn to before me, a notary public, this 15th day of June, 1948.

(Seal) JOHN F. BURNS,

Notary Public in and for the City and County of San Francisco, State of California.

My Commission Expires April 12, 1949.

[Endorsed]: Filed June 21, 1948. [115]

The Tax Court of the United States

Docket No. 9766

GRACE BROS., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between parties hereto through their respective counsel that in addition to the facts admitted by the pleadings

the following facts shall be taken as true, provided however, that this stipulation shall be without prejudice to the rights of either party to introduce other and further evidence not inconsistent with the facts herein stipulated to be taken as true.

1. Petitioner was incorporated under the laws of the State of California on November 22, 1910 and has its principal place of business in the City of Santa Rosa, California.

2. During the year 1943, the petitioner kept its books and records on the accrual basis of accounting and its income tax returns for 1943 were filed on that basis.

3. In 1943, Mr. Joseph T. Grace was the sole stockholder of the petitioner, owning all of its outstanding capital stock. [116]

4. In 1943 and for many years prior thereto the petitioner was engaged in various business enterprises, including farming of various commodities and manufacturing and selling beer.

5. From 1921 to 1942 the petitioner was also engaged in the business of operating a winery, making and selling wine under the trade name of The DeTurk Winery. Some of its wine was sold under the trade name or label of The DeTurk Winery and some was sold in bulk without label. The form of invoice used by petitioner for this business was headed "The DeTurk Winery" and contained the statements "Established 1876" and "Owned by Grace Bros., Inc." Photostat copy of one of said invoices is attached hereto as Exhibit 1-A.

6. During 1941 and 1942 the petitioner sold the

following quantities of wine at an average price per gallon, respectively—

Dry Wine		1941	1942
Bulk	gallons	157,518	114,046
Bottles	gallons	8,888	7,028
Average price per gallon		22.6c	22.2c
Sweet Wine			
Bulk	gallons	46,943	46,009
Bottles	gallons	12,443	10,268
Average price per gallon		37.2c	36.8c

7. All of the petitioner's inventory of wine as of December 31 1942 was produced prior to 1942 excepting 4,959 gallons of white dry wine which were produced in October and November of 1942. [117]

8. On December 30, 1942, the petitioner had an inventory of 522,761 gallons of wine of which 104,000 gallons were delivered on December 31, 1942 to Garrett & Co. as hereinafter stated, leaving a balance of 418,761 gallons as of December 31, 1942 consisting of 248,635 gallons of dry wine and 170,126 gallons of sweet wine, which inventory was carried on the books of the petitioner at \$79,046.33.

9. Attached hereto and marked Exhibit 2-B hereof, is a true copy of a Memorandum of Agreement for Sale and Lease dated January 20, 1943, addressed to Garrett & Co., Inc., Cucamonga, California, by Joseph T. Grace and signed "Jos. T. Grace, doing business as DeTurk Winery."

10. Under this agreement Garrett & Co., Inc. paid \$52,000 to the petitioner computed at 50 cents per gallon for 104,000 gallons of wine delivered to Garrett & Co. by the petitioner in 1942. The petitioner treated this as a sale of 104,000 gallons of wine in 1942 and so reported it on its income tax

return for that year. The petitioner's tax liability for the year 1942 is not involved in this proceeding relating to 1943.

11. Under said agreement Garrett & Co., Inc. also paid to the petitioner during 1943, \$124,317.50 computed at 50 cents a gallon for 248,635 gallons of dry wine; \$94,862.41 computed at 50 cents a gallon for 96,498 gallons of sweet wine and a somewhat higher amount per gallon for 73,628 gallons of sweet wine containing a higher sugar content than required by California standards, all of which wines were delivered by the petitioner to Garrett & Co. during 1943. [118]

12. The respondent has treated the difference between the amount of \$219,179.91 received from Garrett & Co. as aforesaid, and the cost of the wine of \$79,046.33, or \$140,133.58 as profit from sale of wine taxable as ordinary income.

13. Garrett & Co. and the petitioner executed a written lease on January 30, 1943 for the petitioner's winery, together with all wine making machinery and equipment located thereon. A true copy of said lease is attached hereto and marked Exhibit 3-C. The lease provided for a term of 5 years with option exercisable by the Lessee to renew the lease for a similar period.

14. On April 15, 1944, the petitioner released Garrett & Co. from said lease of said winery plant by surrendering the executed lease. Garrett & Co. released and relinquished possession of said winery, and the petitioner sold the said winery plant to Taylor and Company for a price of \$150,000.

15. The escrow covering the transaction was opened with the Sonoma County Land Title Company, Santa Rosa, California, on March 2, 1944. The company delivered its deed of the property to the Taylor Company on April 15, 1944. Taylor and Co. deposited the \$150,000 purchase price on March 7, 1944 and the transaction was completed and the escrow closed by the delivery of the deed to Taylor and Co. and the delivery of the \$150,000 purchase price to Grace Bros., Inc. on April 15, 1944. At no time here material was Taylor & Co. a subsidiary of or owned by Garrett & Co. [119]

16. Grace Bros., Inc. received rentals from Garrett & Co. on the winery property up to and including April, 1944. As soon as the sale of the winery was completed, Mr. Grace returned the executed and cancelled lease to Garrett & Co., and it vacated the winery premises.

17. The petitioner's net income from its winery business from the years 1936 to 1940 is disclosed in the schedule attached hereto and marked Exhibit 4-D. The petitioner's average investment in the assets of its winery business during the period 1936 to 1942 was approximately \$150,000.

18. On or about March 15, 1944, the petitioner filed a California Bank and Corporation Franchise tax return of its income for the calendar year 1943 under the provisions of the California Bank and Corporation Franchise Tax Act, reporting on said return a taxable net income of \$276,030.17 and a franchise tax of \$9,385.03. Copy of said return is attached hereto as Exhibit 5-E. Petitioner paid

said franchise tax of \$9,385.03 during the year 1944. Petitioner did not claim this tax as a deduction on its 1943 Federal income tax return and the respondent has not allowed this tax as a deduction for 1943.

19. Should the Court determine that the said tax is allowable as a deduction for 1943, the amount thereof can be computed after the Court's decision herein and can be given effect in the computation under Rule 50. This issue has been submitted to the Tax Court for decision in the case of Central Investment Corporation, Docket No. 7959.

/s/ GEORGE H. KOSTER,
Counsel for Petitioner.

/s/ J. P. WENCHEL,
Counsel for Respondent. [121]

EXHIBIT 1-A

(Bonded No. 15)

THE DE TURK WINERY

Owned by Grace Bros., Inc.

Established 1876

806 Donahue Street
Santa Rosa, California

March 10, 1942

Sold to: Les Fils de Maurice Cassin, Inc.

Address: Box 4293, Bennett Val Road

City: Santa Rosa, Calif.

Bills Payable at Our Office, Santa Rosa, Calif.

Pkg.	Description	Gallons	Price	Amount
10 bbls.	Saut No. 1	473½	50	246.75
	[Stamp] : De Turk Winery			
	Ship in Bond to			
	Bonded Winery 1262			
	local bulk	[Stamp] : De Turk Winery		
<hr/>				
Total Wine		<hr/>		
License No.		<hr/>		
Calif. Merch. Tax	—Dry	In Bond		
Calif. Merch. Tax	—Swt.			
Federal Tax	—Dry			
Federal Tax	—Swt.			
State Tax	—Dry			
State Tax	—Swt.			
Freight or Drayage		<hr/>		
Total Tax & Freight		<hr/>		
[Figures circled in penciled] : 702 11 703		246.75		
Cooperage		10	5	50.00
<hr/>				
[No. 5237]	(W)	Total Amount		296.75

This Is Your Invoice—No Copy Will Be Sent Unless Requested

Shipment No. 10923

Serial No. 114281-90

Exhibit 1-A—(Continued)

(Bonded No. 15)

THE DE TURK WINERY

Owned by Grace Bros., Inc.

Established 1876

3636

806 Donahue Street
Santa Rosa, California

March 10, 1942

Sold To: A. Figone Co.

Address: 89 Clay St.

City: San Francisco, Calif.

Bills Payable at Our Office, Santa Rosa, California

Pkg.	Description	Gallons	Price	Amount
3 bbls.	Swt Port	149.5	35	52.33
	[Stamp]: De Turk Winery			
	Scioroni bulk			
	[Stamp]: Mar 15 1942 De Turk Winery			
Total Wine				
License No. B 13743 A				
Calif. Merch. Tax	—Dry			
Calif. Merch. Tax	—Swt.	149½	1½	2.24
Federal Tax	—Dry			
Federal Tax	—Swt.	149½	30	44.85
State Tax	—Dry			
State Tax	—Swt.	149½	2	2.99
Freight or Drayage		149½	1½	2.24
Total Tax & Freight				52.32
[Figures circled in pencil]: 702 12				104.65
Cooperage		3	5	15.00
[No. 5238]	Total Amount			119.65

This Is Your Invoice—No Copy Will Be Sent Unless Requested

Shipment No. 10924

Serial No. 114291-93

EXHIBIT 2-B

Santa Rosa, California

January 20th, 1943

Garrett & Company, Inc.,
Cucamonga, California.

Attention: Mr. L. A. Weller, Vice President

Dear Sirs:

The following is a memorandum of agreement for sales and lease agreed upon between the undersigned Joseph T. Grace, doing business as DeTurk Winery, of Santa Rosa, California, and Garrett & Company, Inc., a New York corporation, acting through Mr. L. A. Weller, its Vice-President, to-wit:

Said Jos. T. Grace, has sold and said Garrett & Company, Inc. has bought as of December 31, 1942, 104,000 gallons of wine situate at DeTurk Winery, at Santa Rosa, California, for the sum of \$52,000.00 in cash, the receipt whereof by seller, on January 6, 1943, is hereby acknowledged. Said Jos. T. Grace further agrees to sell and said Garrett & Company, Inc., agree to buy, all of the remainder of that certain inventory of wines now on hand at said De Turk Winery consisting of approximately 416,000 gallons, including both sweet and dry wines, at the purchase price of fifty cents (50c) per gallon. The balance of said wine is to be paid for as said wine is shipped, settlement to be made monthly, provided, however, that not less than 1/10th of the remaining balance of said purchase price is to be paid monthly for the period of ten (10) months from and after this date, and provided further that the whole of

Exhibit 2-B—(Continued)

said purchase price is to be paid in full on or before ten (10) months from this date. The aforesaid 104,000 gallons of wine is to be retained by seller as security for the performance by buyer of this agreement for the purchase of the remaining 416,000 gallons of wine. [123]

It is understood that the inventory of wine sold approximates 520,000 gallons. An inventory of said wine is presently being taken by the authorities of the Internal Revenue Department and such inventory is to be accepted by both buyer and seller as the correct quantity of wine hereby sold.

It is understood that approximately 80,000 gallons of wine contains more sugar than called for by California standards, and that an increased price over and above said purchase price of fifty cents (50c) per gallon is to be paid for such gallonage containing said increased sugar content, the increased price therefor to be computed by A. R. Morrow, of San Francisco, on the accepted standard basis. The buyer shall have thirty (30) days from and after this date to report as to the unsatisfactory condition of any of said wine as being not up to California standards and it is agreed that such gallonage as may be not up to California standards of quality may be deducted from said inventory and retained by the seller. In the event no objection as to quality of wine is made by the buyer within said period of thirty (30) days, such failure to object shall be deemed an agreement on the part of the buyer that all the wine covered in said inventory

Exhibit 2-B—(Continued)

is accepted as of good quality and conforming to California standards.

The buyer Garrett & Company, Inc., agrees to pay all state and county taxes which may be assessed as of March, 1943, as a lien against 150,000 gallons of sweet wine, included in said inventory, and the seller agrees to pay all state and county taxes that may be assessed as of March, 1943, against the remainder of the wine included in said inventory. The buyer further agrees to pay all marketing taxes due the State of California upon said wine as it may be shipped.

The buyer agrees, at its own cost and expense, to pay all fire insurance premiums on said wines from and after the date hereof. The seller further [124] agrees to sell approximately 600 wine barrels now on hand in said winery at the price of Four Dollars (\$4.00) each, it being understood that the seller shall, at his own cost and expense, put said wine barrels in a usable condition satisfactory to the buyer.

The buyer is to be allowed 1% loss for wastage on all wine shipped within said period of ten (10) months from this date, provided that if the total amount of wine as shown by said inventory is received or shipped by the buyer no allowance for wastage shall be made.

It is further understood that said Jos. T. Grace agrees to lease to said Garrett & Company, Inc., the said DeTurk Winery and the adjoining property used for wine making, including all machinery and

Exhibit 2-B—(Continued)

equipment situate on said premises, for the term of five (5) years, commencing January 1, 1943, at an annual rental of Ten Thousand Dollars (\$10,000.00) payable quarterly in advance. Said lessee Garrett & Company, Inc., shall have the privilege and option of renewing said lease for an additional term of five (5) years, at the same rental and upon the same terms upon giving written notice of said option to renew to the lessor not less than six (6) months prior to the expiration of said original term.

The lessee agrees to maintain all of the leased machinery and equipment in good working order and in a reasonable state of repair, allowance being made for ordinary wear and tear. The lessee shall have the right to remove all machinery and equipment installed by it at the expiration of said term, or any extension thereof, such right of removal to expire sixty (60) days after the expiration of said lease, or any renewal thereof. The lessor shall carry at this own expense, all fire insurance on the equipment and building owned by him, and the lessee shall at its own cost and expense carry fire insurance on equipment and machinery that may be installed by said lessee. [125]

The lessor reserves the right to maintain an office of approximately 20 feet by 40 feet in size, adjoining the present winery office, during the term of said lease.

All expense for power and light consumed by the lessee on said premises until separate installations for the account of the lessee can be made, shall be

Exhibit 2-B—(Continued)

prorated on such basis as may be arrived at between the lessor and lessee.

It is agreed that the lessor reserves the right to use of the water from the wells on the leased property for the operation of the cold storage plant adjoining said premises and owned by the lessor. It is further agreed that the lessee, Garrett & Company, Inc., shall have the right to use brine from the adjoining cold storage plant owned by the lessor, at such cost as may be agreed upon between the parties hereto and in the event of their inability to agree, the matter of proper charge for such use shall be submitted to a board of three arbitrators chosen in the usual fashion.

It is understood that the present boilers now situate on said premises are to be placed in such condition by the lessor that the large boiler of approximately 100 horse power can operate at not less than 75 pounds pressure and the smaller 40 horse power at not less than 85 pounds pressure.

The lessor agrees to assign to the lessee for the duration of the lease, and any extension thereof, all rights and privileges in connection with the use of the spur tracks of the Northwestern Pacific Railroad.

It is further understood that said lease is not to be assigned or said premises sublet without the written consent of the lessor.

It is further understood that any and all documents necessary to carry out the foregoing agree-

ment of sale and lease, shall be executed by the parties [126] as soon as it may conveniently be done.

Very truly yours,

JOS. T. GRACE,

Jos. T. Grace, doing business as DeTurk Winery.

Approved and accepted:

GARRETT & COMPANY, INC.,

By L. A. WELLS,

Vice President. [127]

EXHIBIT 3-C

LEASE

This Indenture of Lease, Made this 30th day of January, 1943, by and between Grace Bros., Inc., a California corporation, and Jos T. Grace, hereinafter called "Lessor", and Garrett & Company, Inc., a New York corporation, hereinafter called "lessee",

Witnesseth:

That said lessor, for and in consideration of the rents, covenants and agreements hereinafter mentioned on behalf of the lessee to be paid, kept and performed, does by these presents lease to the said lessee all that certain lot, piece or parcel of land situate lying and being in the City of Santa Rosa, County of Sonoma, State of California, and bounded and particularly described as follows, to-wit:

Commencing at the point where the Southern line of Ninth Street intersects the Eastern line of Donahue Street; thence extending in a Southerly direc-

Exhibit 3-C—(Continued)

tion along Donahue Street, 432 feet; thence in an Easterly direction 178 feet 10 inches to an iron pipe driven in the ground; thence in a Northerly direction 375 feet 10 inches to the Southern line of Ninth Street; thence in a Westerly direction along the Southern line of Ninth Street, 139 feet, 9 inches, to the point of beginning. Being the premises commonly known and described as DeTurk Winery; together with all wine-making machinery and equipment located therein and the right and privilege to use the spur track of the Northwestern Pacific Railroad Company which runs along the Easterly side of said property.

To Have And To Hold the said premises with the appurtenances and said machinery and equipment unto the said lessee, for the term of five years, commencing on the date of issuance by the Internal Revenue Service of Wine Producer's and Blender's Basic Permit to Garrett & Company, Inc., and ending December 31, 1947, reserving, however, unto the lessor the right to maintain an office of approximately 30 feet [128] by 40 feet in size, adjoining the present winery office, during the term of this lease and any extension thereof.

Said lessee agrees to pay, as rental for said premises, the sum of Ten Thousand Dollars (\$10,000.00) annually, payable quarterly in advance in installments of Twenty-five Hundred Dollars (\$2,500.00) each.

Said lessee is hereby given and granted the privilege and option of renewing this lease for an ad-

Exhibit 3-C—(Continued)

ditional term of five years, beginning on the 1st day of January, 1948, at the same rental and upon the same terms and conditions as those herein set forth. Notice of lessee's intention to exercise such option must be given in writing by lessee to lessor not later than the 30th day of June, 1947.

The said lessee does hereby promise to pay the rental herein named and in the manner herein specified. Said lessee also agrees to maintain all of the leased machinery and equipment in good working order and in a reasonable state of repair, allowance being made for ordinary wear and tear.

It is agreed that the lessee shall have the right to remove all machinery and equipment installed by it at the expiration of said term or any extension thereof, such right of removal to expire sixty days after the expiration of said lease or any renewal thereof.

It is further agreed that the lessor shall carry at his expense, all fire insurance on the building and the machinery and equipment owned by him, and the lessee shall, at its own cost and expense, carry fire insurance on equipment and machinery that may be installed by it.

It is further agreed that all expense for power and light consumed by the lessee on said premises until separate installations for the account of the lessee shall be made, shall be prorated on such basis as may be agreed upon between the lessor and lessee and that thereafter [129] the lessee shall pay all

Exhibit 3-C—(Continued)

expenses for power and light consumed by it on the leased premises.

It is further agreed that the lessor reserves the right to use water from the wells on the leased property for the operation of lessor's cold storage plant adjoining said premises and that the lessee shall have the right to use brine from lessor's cold storage plant adjoining said leased premises at such cost as may be agreed upon between the parties hereto. In the event of the inability of said parties to agree upon the price for such brine the matter of proper charges for the same shall be submitted to a board of three arbitrators chosen in the usual fashion.

It is also understood and agreed that the boilers now situate on said leased premises are to be placed in such condition by the lessor that the large boiler of approximately 100 horsepower can operate at not less than 75 pounds pressure and the smaller boiler of approximately 40 horsepower, at not less than 85 pounds pressure.

Lessee agrees not to assign this lease or any part thereof, nor to let or underlet the whole or any part of said premises without the written consent of the lessor first had and obtained; and said lessee hereby waives any right it may have to cancel this lease by reason of failure to obtain tank cars. The provisions of this lease shall extend to and include the executors, administrators, and assigns of lessor Joseph T. Grace and the successors and assigns of the other parties to this lease.

It is further agreed between the parties to these

Exhibit 3-C—(Continued)

presents that in case the premises hereby leased shall be partially damaged by fire, the same shall be repaired with due diligence by the lessor at the lessor's expense; that in case the damages shall be so extensive as to render said premises wholly untenable, the rent hereby reserved shall cease until such time as said premises shall be put in complete repair, [130] but in case of the total destruction of said premises by fire or otherwise, the rent shall be paid up to the time of such destruction, any prepayment refunded, and then and from thenceforth this lease shall cease and terminate.

In Witness Whereof, said parties have executed these presents, in duplicate, the day and year first above written.

GRACE BROS., INC.,

By /s/ J. T. GRACE,

President.

Lessor.

GARRETT & COMPANY, INC.,

By /s/ L. A. WELLER,

Vice President,

Lessee. [131]

	1941	1942
SALES OF WINE	\$ 88,175.96	\$121,491.05
Other Income.....	1,146.12	6,605.83
TOTAL RECEIPTS	\$ 89,322.08	\$128,096.88
WINERY OPERATING EXPENSES		
Labor.....	\$ 5,380.79	\$ 6,134.32
Fuel Oil.....	581.21	607.13
Miscellaneous Supplies.....	1,084.72	629.20
Repairs.....	1,411.36	1,137.05
Insurance.....	2,505.79	.....
Miscellaneous Expenses.....	1,315.81	1,189.64
Depreciation.....	2,571.97	2,949.60
Power Plant.....	1,859.65	2,050.40
Dump Truck.....	53.56	37.75
Taxes.....	2,991.38	4,100.00
Inventory Cost.....	41,077.55	69,115.82
Professional Services.....	.....	.....
	\$ 60,833.79	\$ 87,950.91
WINERY BOTTLING EXPENSES		
Labor.....	\$ 1,316.74	\$ 1,173.70
Supplies.....	6,632.97	4,417.00
Insurance.....	85.94	26.75
Depreciation.....	37.27	.....
Taxes.....	28.62	.....
Inventory Cost.....	6,784.48	4,402.53
Freight.....	.....	.....
	\$ 14,886.02	\$ 10,019.98
SELLING EXPENSES		
Salaries and Commissions.....	\$ 3,418.08	\$ 3,398.80
Advertising.....	410.41	1,243.33
Bad Debts.....	643.11	4,339.90
Miscellaneous.....	304.00	311.02
Hauling and Delivery.....	831.47	1,738.92
Taxes.....	.....	134.49
Dues and Subscriptions.....	.....	.....
	\$ 5,607.07	\$ 11,166.46
TOTAL EXPENSES	81,326.88	109,137.35
NET PROFIT	\$ 7,995.20	\$ 18,959.53

[Endorsed]:

EXHIBIT 4-D
GRACE BROS., INC.
ANALYSIS OF WINERY OPERATIONS
1936 - 1942

	1936	1937	1938	1939	1940	1941	1942
SALES OF WINES.....	\$185,458.03	\$207,539.75	\$102,666.68	\$ 77,805.77	\$ 68,613.15	\$ 88,175.96	\$121,491.05
Other Income.....	.....	846.50	2,145.60	3,840.20	1,064.80	1,146.12	6,605.83
TOTAL RECEIPTS.....	\$185,458.03	\$208,386.25	\$104,812.28	\$ 81,645.97	\$ 69,677.95	\$ 89,322.08	\$128,096.88
WINERY OPERATING EXPENSE							
Labor.....	\$ 7,728.93	\$ 10,342.27	\$ 8,306.96	\$ 4,974.13	\$ 5,433.13	\$ 5,380.79	\$ 6,134.32
Fuel Oil.....	1,791.38	1,182.21	1,062.55	1,452.65	550.69	581.21	607.13
Miscellaneous Supplies.....	2,295.43	747.48	1,091.97	884.59	1,084.72	1,411.36	629.20
Repairs.....	793.03	1,023.29	497.65	590.28	1,391.51	1,315.81	1,137.05
Insurance.....	2,537.47	2,588.76	2,176.56	2,751.99	2,144.65	2,505.79	.....
Miscellaneous Expense.....	.....	.....	2,392.31	1,021.34	1,315.81	1,189.64	.....
Depreciation.....	2,368.30	2,595.06	2,656.44	2,715.24	2,564.62	2,571.97	2,949.60
Power Plant.....	.....	2,288.72	1,813.04	1,474.85	.....	1,859.65	2,050.40
Dump Truck.....	.....	76.04	.....	368.19	24.87	53.56	37.75
Taxes.....	2,184.23	3,014.08	2,212.75	2,603.25	2,307.09	2,991.38	4,100.00
Inventory Cost.....	109,061.77	127,515.20	51,097.72	37,452.80	26,121.89	41,077.55	69,115.82
Professional Services.....	5,948.30	5,314.66	250.00	.....	.....	.....	.....
	\$134,708.84	\$155,940.29	\$ 70,821.15	\$ 57,867.66	\$ 42,444.38	\$ 60,833.79	\$ 87,950.91
WINERY BOTTLING EXPENSE							
Labor.....	\$ 2,523.43	\$ 1,398.63	\$ 2,446.46	\$ 1,475.05	\$ 1,316.74	\$ 1,173.70	.....
Supplies.....	8,450.60	4,580.20	.....	3,930.62	6,632.97	4,417.00	.....
Insurance.....	89.66	105.40	23.16	42.39	85.94	26.75	.....
Depreciation.....	36.36	37.03	37.86	37.27	.....	.....	.....
Taxes.....	30.86	38.60	118.44	71.96	28.62	.....	.....
Inventory Cost.....	.....	.....	.....	5,369.50	6,784.48	4,402.53	.....
Freight.....	2,401.12	.....	.....	.....	.....	.....	.....
	\$ 13,264.73	\$ 13,532.03	\$ 6,159.86	\$ 2,625.92	\$ 10,926.79	\$ 14,886.02	\$ 10,019.98
SELLING EXPENSE							
Salaries and Commissions.....	\$ 4,058.90	\$ 6,456.60	\$ 2,313.23	\$ 2,853.80	\$ 3,418.08	\$ 3,398.80	.....
Advertising.....	232.86	169.65	.....	139.19	410.41	1,243.33	.....
Bad Debts.....	.....	.....	98.39	.....	643.11	4,339.90	.....
Miscellaneous.....	.....	.....	.....	.....	304.00	311.02	.....
Hauling and Delivering.....	246.10	124.34	1,906.92	1,374.37	831.47	1,738.92	.....
Taxes.....	.....	.....	.....	189.56	.....	134.49	.....
Dues and Subscriptions.....	1,191.14	702.76	733.01	1,290.00	.....	.....	.....
	\$ 10,874.28	\$ 7,729.00	\$ 7,453.35	\$ 5,051.55	\$ 5,846.92	\$ 5,607.07	\$ 11,166.46
TOTAL EXPENSE.....	155,847.85	175,201.32	84,434.36	65,545.13	59,218.09	81,326.88	109,137.35
NET PROFIT.....	\$ 26,610.18	\$ 33,184.93	\$ 20,377.92	\$ 16,100.84	\$ 10,459.86	\$ 7,995.20	\$ 18,959.53

[Endorsed]: Filed May 26, 1947. [132]

1121077

UNITED STATES

E. F.

2510

Form 1120
Treasury Department
Internal Revenue Service

CORPORATION INCOME AND DECLARED VALUE EXCESS-PROFITS TAX RETURN 1943

For Calendar Year 1943

or fiscal year beginning 1943, and ending 1944

PRINT PLAINLY CORPORATION'S NAME AND ADDRESS

GRACE TROS. INC.

804 Donahue Street

SANTA ROSA CALIFORNIA

Kind of business: BOOK Mfg.-Book Distribution, Ice-Farming
and Malt.

Business group code number (from instruction 9)

NORMAL-TAX NET INCOME COMPUTATION

GROSS INCOME		
1. Gross sales (where inventories are on income-determining footing)		1,775,125.78
2. Less: Cost of goods sold. (From Schedule A)		1,148,882.92
3. Gross profit from sales		626,242.86
4. Gross receipts (where inventories are not on income-determining footing)		
5. Less: Cost of operations. (From Schedule B)		
6. Gross profit where inventories are not on income-determining footing		
7. Interest on loans, notes, mortgages, bonds, bank deposits, etc.		
8. Interest on corporation bonds, etc.		
9. (a) Interest on United States savings bonds and Treasury bonds owned in excess of \$10,000 (b) Interest on United States bonds owned prior to March 1, 1941. (From Schedule C)		
10. Dividends (From Schedule D)		
11. Rents (From Schedule E)		
12. Royalties (From Schedule F)		
13. Other income (From Schedule G)		
14. Total income in items 1 through 13, inclusive		24,000.00
DEDUCTIONS		
15. Compensation of officers. (From Schedule H)		
16. Salaries and wages (less deducted amounts)		
17. Rent		
18. Depreciation		
19. Bad debts. (From Schedule I)		
20. Interest		
21. Taxes. (From Schedule J) (Deduct declared value excess-profits tax on item 30)		
22. Contributions or gifts paid. (From Schedule K)		
23. Losses by fire, storm, shipwreck, or other casualty, or theft. (Substantiated)		
24. Depreciation. (From Schedule L)		
25. Deductions of mines, oil and gas wells, timber, etc. (Substantiated)		
26. Net operating loss deduction. (Substantiated statement)		
27. Amortization of emergency facilities. (Substantiated schedule)		
28. Other deductions authorized by law. (From Schedule M)		
29. Total deductions in items 15 to 28, inclusive		
30. Net income for declared value excess-profits tax computation (Item 14 minus item 29)		
31. Add: Interest on obligations of certain instrumentalities of the United States issued prior to March 1, 1941. (From Schedule N, line 15 (c) (2) (ii))		
32. Total of item 31 and 30		
33. Less: Declared value excess-profits tax		
34. Net income		
35. Less: Interest on certain obligations of the United States and its instrumentalities issued prior to March 1, 1941. (From Schedule O, line 9 (a) and 22)		
36. Adjusted net income		
37. Less: Income subject to excess profits tax. (From Form 1121)		
38. Dividends received credit (25 percent of column 2, Schedule E, but not in excess of 25 percent of item 37 minus item 36, above)		
39. Normal-tax net income		

TOTAL INCOME AND DECLARED VALUE EXCESS-PROFITS TAXES

40. Total income tax (line 38 or 39, page 2, whichever is applicable)	
41. Less: Credit for income taxes paid to a foreign country or United States possession or to a domestic corporation	
42. Balance of income tax	
43. Total declared value excess-profits tax (line 8, page 2)	
44. Total income and declared value excess-profits taxes due	

AFFIDAVIT. (See instruction 12)
We, the undersigned, president (or vice president, or other principal officer) and treasurer (or other officer) of this corporation, do hereby certify that the information furnished in this return, including the schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and correct statement of the facts for the taxable year ended, pursuant to the Internal Revenue Code and the regulations issued thereunder.

Subscribed and sworn to before me this 1943 day of June.

NOTARIAL SEAL

NOTARY PUBLIC

(Title)

AFFIDAVIT. (See instruction 12)

I/we (swear) (or affirm) that I/we prepared this return for the person named herein and that the return (including any accompanying schedules and statements) is a true, correct, and complete statement of all the information respecting the tax liability of the person for whom this return has been prepared.

Subscribed and sworn to before me this 1943 day of June.

NOTARIAL SEAL

NOTARY PUBLIC

JACK LICHAN AND ASSOCIATES

Net income for declared value excess-profit tax computation (line 31, page 1)

Value of capital stock owned by your capital stock last return for the year ended June 30, 1960 for your capital stock in 1964, if your business had total your report for 1964, as indicated on your July 1, 1964, statement

10 percent of line 2

Dividends received credit (85 percent of column 2, Schedule F, part one in excess of \$5 percent of item 37 minus item 38, page 1)

Balance subject to declared value excess-profit tax (line 1 minus total of lines 4 through 6)

Amount taxable at 6.5 percent (5 percent of line 2, but not more than line 5; or 6 percent of line 6)

Balance taxable at 12.5 percent (line 5 minus line 6, column 1), and tax

Total declared value excess-profit tax (total of line 6, column 3, and line 7)

\$ 2,000.
\$ 800.
\$ 1,200.

Table 1		Table 2	
A summary of the		A summary of the	
\$ 272,003 66			
\$ 200,000 00			
\$ 72,003 66			
\$ 72,003 66	4.8 %	\$ 4,752 26	
\$	13.2 %	\$ 4,752 26	

INCOME TAX COMPUTATION. (See Computation Instructions)

DOMESTIC CORPORATIONS WITH FEDERAL-TAX NET INCOME FOR 1994

23. Normal-tax net income (Item 40, page 1).
24. Portion of line 9 (not in excess of \$5,000); and tax at 15 percent.
25. Portion of line 9 (in excess of \$5,000 and not in excess of \$20,000); and tax at 17 percent.
26. Portion of line 9 (in excess of \$20,000 and not in excess of \$25,000); and tax at 19 percent.
27. Portion of line 9 (in excess of \$25,000); and tax at 21 percent.
28. Total normal tax (total tax in column 8 of lines 10, 11, 12, and 13).

1	15%
2	17%
3	19%
4	21%

DOMESTIC COMPANIES WITH NORMAL-TAX NET INCOME OF OVER \$100,000 AND FOREIGN CORPORATIONS INCURRED IN DOMESTIC
GAINS, THE UNITED STATES INDISPENSIVE OF AMOUNT OF NORMAL-TAX NET INCOME

18. Normal-tax net income (Item 48, page 1) _____
19. Normal tax (24 percent of line 18) _____

224,511	24	50,000	91
---------	----	--------	----

NETAL CONCENTRATION

17. Net income (Item 26, page 1) _____
18. Less: Income subject to excess profits tax _____
19. Dividends received credit 80 percent of column 1, Schedule E (excluding _____
20. Dividends received credit on preferred stock of a public utility), but _____
- not to exceed 80 percent of line 17 income less _____
21. Dividends paid on certain preferred stock E taxpayer is a public utility _____
22. Excess net income _____

8	25281	62
	43090	38
	22727	27

CONCURRENCE WITH FERTALITY AND MENSTRUATION MAY BE AN

22. Portion of line 21 (not in excess of \$25,000); and tax at 10 percent (or 12 percent in the case of a consolidated return)
23. Portion of line 21 (in excess of \$25,000 and not in excess of \$50,000), and tax at 22 percent (or 24 percent in the case of a consolidated return)
24. Total net tax in column 3 of lines 22 and 23

1		10%
		22%

CORRELATIONS WITH INITIAL KEY NUMBER OF CRYA INDEX

26. Surtax (16 percent of line 25) (or in the case of a consolidated return, 16 percent of the consolidated surtax net income)
27. Total normal and surtax (Lines 14 or 16, plus line 26 or 28, whichever is applicable)
28. Total tax (Lines 27 and line 23, Schedule C)

1. 224, 211 22		1. 224, 211 22
dated earlier not income)	10%	1. 224, 211 22
		1. 224, 211 22
		1. 224, 211 22

TAX COMPUTATION FOR REGULATED INVESTMENT COMPANIES

20. Adjusted net income (Item 27, page 1, but computed without regard to section 47 (a)).
21. Add: Net operating loss deduction (Item 27, page 1)
22. Total of lines 20 and 21
23. Less: Excess of net long-term capital gain over short-term capital loss. (From Schedule C)
24. Adjusted net income (after applying section 262 (b) (1)).
25. Less: Basic surtax amount (including capital gain dividends) computed without regard to paragraphs (3) and (3) of section 27 (g). (Submitt schedule)
26. Supplement Q net income
27. Normal tax (24 percent of line 25)
28. Net income (Item 26, page 1, but computed without regard to section 47 (a)).
29. Add: Net operating loss deduction (Item 27, page 1)
30. Total of lines 27 and 28
31. Less: Excess of net long-term capital gain over short-term capital loss. (From Schedule C)
32. Net income (after applying section 262 (b) (3)).
33. Less: Dividends (other than capital gain dividends) paid including consent dividends credit. (Submitt schedule)
34. Supplement Q surtax net income
35. Surtax (10 percent of line 33)
36. Net long-term capital gain. (From Schedule C)
37. Less: Net short-term capital loss. (From Schedule C)
38. Capital gain dividends paid. (Submitt schedule)
39. Excess subject to tax
40. Tax (26 percent of line 38)
41. Total tax in lines 26, 44, and 49

[illegible]**Schedule A.—COST OF GOODS SOLD.** (See instruction 2)

EXHIBIT A—COST OF GOODS SOLD. (See page 10)
(These amounts are in thousands of dollars)

Inventory at beginning of year	174,409	80
Material or merchandise bought for manufacture or sale	762,643	78
Salaries and wages	294,540	26
Other costs per books. (Attach itemized schedule)	13,681	40
Total	1,245,273	84
Less: Inventory at end of year	99,426	87
Cost of goods sold (enter as Item 2, page 1)	1,145,847	97

Schedule B.—COST OF OPERATIONS

MINIMUM INVESTMENT OF OPERATION

Salaries and wages		
Other costs (to be detailed):		
(a)		
(b)		
(c)		
(d)		
(e)		
Total (enter as item 5, page 1)		

Schedule C.—Separate Schedule C (Form 1120) should be attached and used in reporting sales and exchanges of capital assets and that with and is a part of this return.

Schedule D.—GAINS AND LOSSES FROM SALES OR EXCHANGES OF PROPERTY OTHER THAN CAPITAL ASSETS. (See instruction 13)

1. Description of Property	2. Date Acquired	3. Gross Sales Price (Contract price)	4. Cost or Other Basis	5. Expense of Sale and Cost of Improvements Incurred from Acquisition to March 1, 1913	6. Depreciation Allowed (or allowable) Since Acquisition on March 1, 1913 (Provide details)	7. Gain or Loss Realized on Sale of March 1, 1913 (Provide details)

Supplemental information required for Schedule D

State with amount to each item of property reported to Schedule D (1) how property was acquired

(*) Share with respect to each date of property received in Schedule D: (i) how property was acquired; (ii) whether purchase was a corporation other than that of personal services; (iii) if purchased or otherwise indirectly owned by one or more individuals or by for the same individual or his family; and (iv) where purchaser was a corporation, whether owner.



L. Name and Address of Paying Corporation.

4. Name and address of Paying Corporation		5. Federal Corporation Income Tax Return for the year ending 12/31/	6. Other Corporations
<div style="border: 1px solid black; height: 100px; width: 100%;"></div>		<div style="border: 1px solid black; height: 100px; width: 100%;"></div>	<div style="border: 1px solid black; height: 100px; width: 100%;"></div>
Totals			
Total of columns 2, 3, and 4. (Enter as item 13, page 1 of Form 1000)			

Dividends on share amounts in Federal savings and loan associations in case of share amounts issued prior to March 28, 1942, should not be listed, but the amount should be included in items 11 and 12.

Schedule F.—COMPENSATION OF OFFICERS

1. Name and Address of Officer	2. Official Title	3. Term Devoted to Business	Percentage of Corporation's Stock Owned		4. Cash	5. Other
			4. Common	4. Preferred		
Joe. T. Grace	Pres				\$ 6,000	00
Total compensation of officers. (Enter as item 16, page 1)					\$	00

Note:—Schedule F-1 (IN DUPLICATE) also must be filed with this return if compensation in excess of \$75,000 was paid to any officer or employee.

Schedule C.—BAD DEBTS. (See instruction 26) (See notes 1 and 2)

3. Fugitive Year	5. Hot Income Reported	4. Sales on Account	6. Bad Debts of Corporation if No Reserve is Carried on Books (See note 2)	7. Corporation Credits a Reserve—	
				5. Gross Amount Added to Reserve	6. Amount Charged Against Reserve
1938					
1939					
1941					
1942					
1943					

1. Check whether deduction claimed represents debts which have become worthless ☐ or is an addition to a reserve ☐.

2. Not including securities which are capital assets and which became worthless within the taxable year. Such securities which became worthless within the year should be reported in Schedule C.

Schedule H—TAXES (See instruction 22)

Debit	Credit
Capital Stock Retainable Tax M. E. Thompson & Son Inc Real Estate Personal Property Comp. Insurance Licenses	Amount 2,800 00 4,025 89 11,544 17 10,635 87 3,749 56 4,635 02 2,069 45
Total (Brought from Item 22, page 1)	

~~Section 1. CONTRIBUTIONS OR GIFTS PAID. (See Instruction 2)~~

Name and Address of Contribution	Amount
Floor Tax	634 74
Fed. Stamp-Drawery	274,880 00
Beverage Tax	22,406 25
Sales Tax	229 20
Total Taxes	298,150 19
Total (Enter as item 22, page 1, subject to 3 percent limitation.) (See Instruction 22)	

Schedule J.—DEPRECIATION. (See Instruction 25)

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Cost or Other Basis (Do not include land or other nondepreciable property)	4. Annual Policy Exp. reported in Part III at End of Year	5. Depreciation Allowed (See instructions) to First Year	6. Remaining or Estimated Basis for Accounting	7. Estimated Salvage Value (If any) at End of Depreciation Period	8. Estimated Residual Value From Beginning of Year	9. Depreciation Allowed This Year
Buildings	Year	194		38,217 86	109,497 87	87	12	6,882 84
Bureau Building	1942	178,000 00	\$	19,000 00	159,000 00	30	30	1,000 00
Bureau, Inc.	6-1942	30,000 00		3,000 00	27,000 00	500	500	2,800 00
Bureau, Inc. Building	6-1942	28,000 00		107,497 87	27,500 00	10	99	21,700 00
Bureau Building	1942	30,000 00			30,000 00	10	Var	2,000 00
Antennas & Towers	Var	375 35		318 01	55 34	Var	Var	None
Truck	1942	1,800 00		None	1,800 00	4	24	225 00
Total (Enter on Item 23, page 1)	1942	414,971 12		140,017 94	274,953 18			41,847 84

Schedule E—OTHER DEDUCTIONS. (See instruction 27)

QUESTIONS

1. Date of incorporation December 22, 1910
California
 2. State or country
 3. State collector's office where the corporation's return for the preceding year was filed. San Francisco
 4. The corporation's books are in care of Office
 Located at 806 Donahue Street
 5. Number of places of business Three
 6. Did the corporation during the taxable year have any Government contracts or subcontracts? Yes or "No"? No. If answer is "yes" state the approximate aggregate gross dollar amount billed during the taxable year under all such contracts and/or subcontracts. (See Instruction G-5) 1
 7. Is the corporation a personal holding company within the meaning of section 501 of the Internal Revenue Code? Yes (If so, an additional return on Form 1120 H must be filed.)
 8. Is this a consolidated return? No. (If so, procure from the collector of the district for your district Form 111, Affiliated Schedule, which should be filed in, sworn to and filed as a part of the return.)
 9. If this is not a consolidated return, did you own at any time during the taxable year 50 percent or more of the voting stock of another corporation either domestic or foreign? No; or (b) did any corporation individual partnership, trust, or association own at any time during the taxable year 50 percent or more of your voting stock?
 If either answer is "yes" attach separate schedule showing: (1) Name and address; (2) percentage owned; (3) name of corporation.

stock was acquired; and (4) the collector's office in which the income tax returns of such corporation, individual, partnership, trust, or association for the last taxable year was filed.)

- 10 Is this return made for the calendar year? **Yes** (You may check.)
- 11 Did the corporation at any time during its taxable year have in its company more than eight individuals?
- (Answer "yes" or "no") **Yes** . . . If answer is "yes," has the corporation in this return taken a deduction for any amount of wages paid or other compensation reported at increased or decreased rate? (Answer "yes" or "no") If answer to second question is "yes," attach statement explaining all such increases or decreases. If any of such increases or decreases required the prior approval of the National War Labor Board, attach a copy of the order of the Board. If no such order is stated in Instruction 16, attach also a copy of the authorization for each of such increases or decreases.
- 12 State whether the inventories at the beginning and end of the taxable year were taken at cost or at market, whichever is lower.
- Cost or Market** If other basis is used, explain fully in separate statement. Using date inventory was last reconciled with
- 13 Did the corporation make a return of information on Form 1099 as required by Regulations V-2 and W-2 for the calendar year 1943? (See Instructions.)
- Yes**
- 14 Did the corporation at any time during the taxable year own directly or indirectly any stock of a foreign corporation? (Answer "yes" or "no")
- No** If answer is "yes," attach statement as required by Instruction K(2).

	Beginning of Taxable Year		End of Taxable Year	
	Amount		Amount	Total
ASSETS				
1. Cash		\$ 27,297 94		\$ 149,862 07
2. Notes and accounts receivable				
Less: Reserve for bad debts		84,185 62		171,096 12
3. Inventories (itemize in separate schedule)				
4. Investments in governmental obligations Livestock		174,403 40		99,426 67
(a) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia, or United States possessions		1,403 25		
(b) Obligations of the United States				
(1) Obligations issued on or before September 1, 1917, all postal savings bonds; Treasury notes issued prior to December 1, 1940, and Treasury bills issued prior to March 1, 1941				
(2) United States savings bonds and Treasury bonds issued prior to March 1, 1941				
(3) Treasury notes issued on or after December 1, 1940, and all other obligations of the United States issued on or after March 1, 1941				50,000 00
(c) Obligations of instrumentalities of the United States				
(1) Obligations of Federal land banks, joint stock land banks, and Federal intermediate credit banks issued prior to March 1, 1941				
(2) Obligations issued by other instrumentalities of the United States prior to March 1, 1941				
(3) Obligations of all instrumentalities of the United States issued on or after March 1, 1941				50,000 00
5. Other investments (itemize)		268,425 00		268,425 00
6. Capital assets: Buildings & Equipment	144,444 16		163,493 10	
(a) Depreciable assets (itemize in separate schedule)	182,322 54		251,478 02	
Less: Reserve for depreciation				
(b) Depreciable assets	326,766 70		414,971 12	
Less: Reserve for depletion depreciation	140,017 94	186,746 76	171,860 44	245,106 66
(c) Land	5,550 00	50,964 39	13,815 00	59,244 39
7. Other assets (itemize) Revenue Stamp	598 00		5,550 00	
Due from Affl. C. etc.	121,366 69	127,215 29		16,148 00
8. TOTAL ASSETS		\$ 928,647 65		\$ 1,008,900 33
LIABILITIES				
9. Accounts payable		23,207 88		46,144 07
10. Bonds, notes, and mortgages payable:				
(a) With original maturity of less than 1 year	\$ 34,957 07			
(b) With original maturity of 1 year or more	2,490 22	37,447 38		
11. Accrued expenses (itemize) Taxes	1,477 56			
Other	23,000 00	24,477 56		
12. Other liabilities (itemize) Advances F.T.C.	67,003 56			
Suspense		67,003 56		4,921 85
13. Surplus reserves (itemize in separate schedule)				
(a) Preferred stock				
(b) Common stock		50,000 00		50,000 00
14. Paid-in or capital surplus		101,863 74		101,863 74
15. Earned surplus and undivided profits		622,444 06		622,444 06
17. TOTAL LIABILITIES		\$ 928,647 65		\$ 1,008,900 33

Schedule M.—RECONCILIATION OF NET INCOME AND ANALYSIS OF EARNED SURPLUS AND UNDIVIDED PROFITS

1. Total distributions to stockholders charged to earned surplus during the taxable year:			12. Earned surplus and undivided profits at close of preceding taxable year (Schedule L)	\$ 622,444 06
(a) Cash			14. Adjusted net income (Item 27, page 1)	\$ 779,029 82
(b) Stock of the corporation			15. Nontaxable and partially exempt income:	
(c) Other property			(1) Interest on:	
2. Contributions (excess over 3 percent limitation)			(a) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia, or United States possessions	
3. Federal income and excess-profits taxes	42,451 58		(2) Obligations of the United States:	
4. Income taxes claimed as a credit in whole or in part in Item 42, page 1			(i) Obligations issued on or before September 1, 1917; all postal savings bonds; Treasury notes issued prior to December 1, 1940; and Treasury bills issued prior to March 1, 1941	
5. Federal taxes paid on tax-free covenant bonds			(ii) United States savings bonds and Treasury bonds owned in the principal amount of \$5,000 or less, issued prior to March 1, 1941	
6. Excess of capital losses over capital gains			(iii) United States savings bonds and Treasury bonds owned in excess of the principal amount of \$5,000 issued prior to March 1, 1941	
7. Additions to surplus reserves (list separately):			(4) Obligations of instrumentalities of the United States:	
(a)			(i) Obligations of Federal land banks, joint stock land banks, and Federal intermediate credit banks issued prior to March 1, 1941	
(b) Contributions	150 00		(ii) Obligations issued by other instrumentalities of the United States prior to March 1, 1941	
8. Other unallowable deductions:			(b) Other nontaxable income (itemize):	
(a)			(1)	
(b)			(2)	
9. Adjustments not recorded on books (itemize):			16. Charges against surplus reserves (itemize):	
(a)			17. Adjustments not recorded on books (itemize):	
(b)			18. Sundry credits to earned surplus (itemize):	
10. Sundry debits to earned surplus (itemize):			19. Total of lines 12 to 18	\$ 894,449 85
(a)				
(b)				
11. Earned surplus and undivided profits at close of the taxable year (Schedule L)	651,868 55			
12. Total of lines 1 to 11	\$ 894,449 85			

EXCESS PROFITS TAX. (See Instructions for Form 1121)

- (a) Is an excess profits tax return on Form 1121 being filed for the taxable period covered by Form 1121?
- (b) If a personal service corporation (other than a member of an affiliated group of corporations filing a consolidated return) signifies below its name not to be subject to the excess profits tax, it shall be exempt from such tax and the provisions of Supplement A, Chapter 1, shall apply to the shareholders in such corporation who were such shareholders on the last day of the taxable year of the corporation. (Attach Form 1121-5B)
- (c) If corporate status exemption under section 727 of the Internal Revenue Code, on a state basis of claim is claimed, the following Schedule N does not constitute the filing of an excess profits tax return.

Schedule N.—EXCESS PROFITS NET INCOME COMPUTATION

1. Normal-tax net income (computed without credit for income subject to excess profits tax) (Item 40 plus Item 38, page 1)			6. Dividends received (net of adjustment from Item 12, page 1, and the net of a dividend received netted or subtracted in an excess profits netting computation, and the first \$100 of such stock held primarily for sale to customers by a bank or insurance company, as such stock is, page 1)	
2. Net short-term capital gain (do not enter net short-term capital loss)			7. Net gain from sale or exchange of capital assets (Item 12, page 1)	
3. 50 percent of interest on borrowed capital			8. Income from retirement or discharge of bonds, etc.	
4. Adjustment to net operating loss deduction under section 711 (a) (2) (L)			9. Refunds and interest on Agricultural Adjustment Act loans	
5. Total of lines 1 to 4			10. Recoveries of bad debts	
			11. Total of lines 5 to 10	



GRACE WINE. INC.
1948 INCOME TAX RETURN

OTHER COSTS--SCHEDULE "A"

Ice. Mfg.	\$ 631.25
Distillery Exp.	5.62
Winery	1,085.05
Patchett Ranch	6,219.35
Winebar	4,521.22
Fulton	912.47
Dehydrator	246.54
	<u>\$ 15,621.48</u>

OTHER DEDUCTIONS--LINE 29

Salesman & Driver Exp.	\$ 17,518.32
General Brewery Exp.	3,609.72
Gas & Oil	6,497.65
Stationery & Postage	1,650.10
Adv.	962.81
Buss and Sub.	1,208.55
Power and Water	14,022.17
Supplies-Calif. Ice	4,095.45
Delivery Expense Calif. Ice	1,519.40
Freight	20,256.21
Telephone	3,453.35
Traveling	3,608.99
Trade Allowances	449.90
Repairs	564.25
Winery Bottling Exp.	490.63
Wine Selling Exp.	506.78
S. E. Administrative Exp.	3,230.17
Insurance	<u>12,657.40</u>
	\$ 96,321.83

2510

Loss-Inventory adjustment
Journalized in cost of sales-
material

74,976.55

Line 29-Other Deductions

\$ 21,345.30



UNITED STATES SCHEDULE OF CAPITAL GAINS AND LOSSES For Calendar Year 1943

Or fiscal year beginning _____, 1943, and ending _____, 1944

(Insurance companies using this form should follow notes 1 to 3, inclusive)

<p>This schedule must be filed with and as a part of the corporation's income tax return, Form 1120 or Form 1120 M, for the taxable year, in case of sale or exchange of capital assets.</p>	<p>PRINT PLAINLY CORPORATION'S NAME AND ADDRESS</p> <p>GRACE HERB. INC. (Name) 806 DONAHUE STREET (Street and number) SANTA ROSA CALIFORNIA (Post Office and State)</p>	<p>Do not file this form if the corporation did not sell or exchange any capital assets during the taxable year.</p>
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1. Description of Property	2. Date Acquired	3. Gross Sales Price (or cost or other basis)	4. Cost or Other Basis	5. Expense of Sale and Cost of Improvements (Statement to Acquisitions or March 1, 1943)	6. Depreciation Allowed (or allowable) Since Acquisition or March 1, 1943 (Form 213)	7. Gain or Loss (Enter in plus column if gain, minus column if loss)
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SHORT-TERM CAPITAL GAINS AND LOSSES—ASSETS HELD FOR NOT MORE THAN 6 MONTHS

Total net short-term capital gain (or loss)						

LONG-TERM CAPITAL GAINS AND LOSSES—ASSETS HELD FOR MORE THAN 6 MONTHS

Date	Variation	\$ 219,179.91	\$ 72,046.55			\$ 140,133.36
DeLusk Winery sold out to Garrett E. Hiram Walker						
Total net long-term capital gain (or loss)						\$ 140,133.36

SUMMARY OF CAPITAL GAINS AND LOSSES

1. Classification	2. Gain or Loss in or to Taxes Due Account	
	(a) Gain	(b) Loss
1. Total net short-term capital gain (or loss) from column 7, above	\$ 140,133.36	\$
2. Total net long-term capital gain (or loss) from column 7, above	\$ 140,133.36	\$
3. Net capital loss carry-over (attach statement)	\$	\$
4. Net gain in column 2, lines 1, 2, and 3 (Enter as item 12 (a), page 1, Form 1120)	\$ 140,133.36	\$
5. Net loss in column 2, lines 1, 2, and 3 (No net loss allowable)	\$	\$

COMPUTATION OF ALTERNATIVE TAX

USE ONLY IF THERE IS AN EXCESS OF NET LONG-TERM CAPITAL GAINS OVER NET SHORT-TERM CAPITAL LOSSES

1. Net income (item 35, page 1, Form 1120)	\$ 267,811.04
2. Net long-term capital gain (line 2, column 2 (a), of summary above)	\$ 140,133.36
3. Less: Net short-term capital loss (line 1, column 2 (b), plus line 3, of summary above)	\$
4. Excess of net long-term capital gain over net short-term capital loss	\$ 140,133.36
5. Net income reduced by excess in line 4 (line 1 minus line 4)	\$ 127,677.68
6. Less: Interest on certain obligations of the United States and its instrumentalities issued prior to March 1, 1941 (Item 36, page 1, Form 1120)	\$
7. Adjusted net income (line 5 minus line 6)	\$ 127,677.68
8. Less: Income subject to excess profits tax (item 38, page 1, Form 1120)	\$ 43,040.38
9. Dividends received credit (85 percent of column 2, Schedule E, but not in excess of 85 percent of item 37, minus item 38, page 1, Form 1120)	\$ 43,040.38
10. Balance subject to normal tax	\$ 84,637.30

NORMAL TAX COMPUTATION

DOMESTIC CORPORATIONS WITH NORMAL-TAX NET INCOME OR NET LOSS

Column 1	Column 2
11. Adjusted normal-tax net income (line 10)	\$ 84,637.30
12. Portion of line 11 (not in excess of \$5,000); and tax at 18 percent	18%
13. Portion of line 11 (in excess of \$5,000 and not in excess of \$20,000); and tax at 17 percent	17%
14. Portion of line 11 (in excess of \$20,000 and not in excess of \$25,000); and tax at 19 percent	19%
15. Portion of line 11 (in excess of \$25,000); and tax at 21 percent	21%
16. Total normal tax (total tax in column 2 of lines 12, 13, 14, and 15)	\$

DOMESTIC CORPORATIONS WITH NORMAL-TAX NET INCOME OVER \$25,000 AND FOREIGN CORPORATIONS INCURRED BY BUSINESS WITHIN THE UNITED STATES (EXCEPTIVE OF AMOUNT OF NORMAL-TAX NET INCOME)

17. Adjusted normal-tax net income (line 10)	\$ 84,637.30
18. Normal tax (24 percent of line 17)	24%

SURTAX COMPUTATION

19. Net income from line 5, above	\$ 127,677.68
20. Less: Income subject to excess profits tax	\$
21. Dividends received credit (85 percent of column 2, Schedule E, excluding certain dividends received on preferred stock of a public utility), but not in excess of 85 percent of line 17 minus line 18, page 2, Form 1120	\$
22. Dividends paid on certain preferred stock if taxpayer is a public utility	\$
23. Adjusted surtax net income	\$ 84,637.30

CORPORATIONS WITH SURTAX NET INCOME NOT OVER \$25,000

24. Portion of line 23 (not in excess of \$25,000); and tax at 10 percent (or 15 percent in the case of a consolidated return)	10%
25. Portion of line 23 (in excess of \$25,000 and not in excess of \$50,000); and tax at 22 percent (or 24 percent in the case of a consolidated return)	22%
26. Total surtax in column 2 of lines 24 and 25	\$

CORPORATIONS WITH SURTAX NET INCOME OVER \$25,000

27. Adjusted surtax net income (line 23)	\$ 84,637.30
28. Surtax (16 percent of line 27) (or 18 percent in the case of a consolidated return)	16%
29. Partial tax (line 16 or 18 plus 26, or 28, whichever is applicable)	\$ 15,458.43
30. 25% of line 4	\$ 35,033.36
31. Alternative tax (line 29 plus line 30)	\$ 50,491.79
32. Total normal tax and surtax (line 27, page 2, Form 1120)	\$ 99,684.48
33. Tax liability (line 31 or 32, whichever is lower). (Enter as line 28, page 2, Form 1120)	\$ 50,491.79

Notes: 1. Corporation taxable on net income. 2. See instructions on page 1120. 3. See instructions on page 1120. 4. See instructions on page 1120. 5. See instructions on page 1120. 6. See instructions on page 1120. 7. See instructions on page 1120. 8. See instructions on page 1120. 9. See instructions on page 1120. 10. See instructions on page 1120. 11. See instructions on page 1120. 12. See instructions on page 1120. 13. See instructions on page 1120. 14. See instructions on page 1120. 15. See instructions on page 1120. 16. See instructions on page 1120. 17. See instructions on page 1120. 18. See instructions on page 1120. 19. See instructions on page 1120. 20. See instructions on page 1120. 21. See instructions on page 1120. 22. See instructions on page 1120. 23. See instructions on page 1120. 24. See instructions on page 1120. 25. See instructions on page 1120. 26. See instructions on page 1120. 27. See instructions on page 1120. 28. See instructions on page 1120. 29. See instructions on page 1120. 30. See instructions on page 1120. 31. See instructions on page 1120. 32. See instructions on page 1120. 33. See instructions on page 1120.



QUESTIONS

- (a) Date of incorporation November 22, 1910 (b) State or country California
 (c) Collector's office in which your income tax return for the taxable year was filed San Francisco
 (d) Is this a consolidated return? No If so, procure from the collector Form 851, Affiliations Schedule, which shall be filled in, sworn to, and filed as a part of the consolidated income tax return.
 (e) In computing the excess profits credit under the invested capital method, do you elect to include in excess profits net income interest received on, reduced by the amount of amortizable bond premium under section 125 attributable to, all Government obligations described in section 22(b)(4) of the Internal Revenue Code? (Answer "yes" or "no")
 (f) Are you a transferor or transferee upon an exchange as defined by section 760 or 761 of the Internal Revenue Code? (Answer "yes" or "no")
 (g) Does this return involve an adjustment of the excess profits tax liability due to the application of the sections specified in (1) below? (Answer "yes" or "no") If answer is "yes":
 (1) Check the appropriate sections and submit schedules showing computation: 710(a)(4) ☐ 721 ☐ 726 ☐ 731 ☐ 735(b) ☐ 735(c) ☐ 736(a) ☐ 736(b) ☐ (See General Instructions E, 1, G, H, and I.) (Enter amount of excess profits tax as item 18 (b), page 1.)
 (2) From the schedules submitted under (1) above, enter any tax adjustment which results from the application of each of the following sections:
 721, \$; 726, \$; 731, \$;
 (3) From the schedules submitted under (1) above, enter any income adjustment which results from the application of each of the following sections:
 721, \$; 731, \$; 735(b), \$; 735(c), \$
 (h) State amount of total assets as of the end of the taxable year. (From Form 1120, page 4, line 8, last column), \$

Schedule A. EXCESS PROFITS NET INCOME COMPUTATION

	Column 1 INCOME METHOD	Column 2 INVESTED CAPITAL CREDIT METHOD
1. Normal-tax net income (computed without allowance of credit for income subject to excess profits tax and without allowance of dividends received credit) (item 37, page 1, Form 1120).....	\$	\$ 267,251 62
2. Net short-term capital gain (do not enter net short-term capital loss).....		
3. Adjustment to net operating loss deduction.....		
4. Decrease in deductions limited by income.....		
5. 50 percent of interest on borrowed capital.....	XXXXXXXX XX	
6. Interest on Government obligations (see question (e) above, for election).....	XXXXXXXX XX	
7. Total of lines 1 to 6.....	\$	\$ 267,251 62
8. Net gain from sale or exchange of capital assets (item 12 (a), page 1, Form 1120).....	\$	\$ 140,135 58
9. Income from retirement or discharge of bonds, etc.....		
10. Refunds and interest on Agricultural Adjustment Act taxes.....		
11. Recoveries of bad debts.....		
12. Increase in deductions limited by income.....		
13. (a) Dividends received credit adjustment (item 13, page 1, Form 1120, excluding dividends received from foreign corporations).....		XXXXXXXX XX
(b) Dividends received credit adjustment (item 13, page 1, Form 1120, excluding dividends received from foreign personal holding companies and dividends received on stock held primarily for sale to customers by a dealer in securities).....	XXXXXXXX XX	
14. Nontaxable income of certain industries with depletable resources.....		
15. Total of lines 8 to 14.....		\$ 140,135 58
16. Excess profits tax net income computed without regard to deductions applicable to life insurance companies (line 7 minus line 15).....	\$	\$ 127,118 04
17. Deductions applicable to life insurance companies.....		
18. Excess profits net income computed under income credit method or invested capital credit method (line 16, or line 16 minus line 17 in case of a life insurance company).....	\$	\$ 127,118 04

Schedule C—EXCESS PROFITS CREDIT—BASED ON INVESTED CAPITAL

Equity Invested Capital at the Beginning of the Taxable Year (See instructions for Schedule C, lines 1 to 12, included)				
Money paid in for stock, or as paid-in surplus, or as a contribution to capital		\$	80,000	00
Property paid in for stock, or as paid-in surplus, or as a contribution to capital		\$	101,946	76
Distributions of earnings and profits in stock of the corporation				
(a) Accumulated earnings and profits		\$		
(b) Adjustment for transferor's deficit under section 718 (e) (5)		\$		
(c) Increase or decrease under section 761 (d) (1) on account of intercorporate liquidation		\$		
(d) Accumulated earnings and profits (item 4 (a)) as adjusted by item 4 (b) and (c)		\$	222,445.00	Less 43,431.35
25 percent of new capital paid in during a taxable year beginning after December 31, 1940				00
Increase on account of intercorporate liquidation under section 761 (d) (2)				00
Deficit in earnings and profits of another corporation under section 718 (a) (7)				00
Total of lines 1 to 7		\$	281,014	43
Less: Distributions made prior to the taxable year not out of accumulated earnings and profits		\$		
Earnings and profits of another corporation required to be deducted by section 718 (b) (3)				
Decrease on account of intercorporate liquidation under section 761 (d) (3)				
Deficit in earnings and profits in invested capital of another corporation (section 718 (b) (5))				
Total of lines 9 to 12				
Equity invested capital at beginning of taxable year (line 8 minus line 13)		\$	281,014	43
Average Addition to Equity Invested Capital During the Taxable Year (See instructions for Schedule C, lines 1 to 12, included)				
Money paid in for stock, or as paid-in surplus, or as a contribution to capital		\$		
Property paid in for stock, or as paid-in surplus, or as a contribution to capital				
Distributions of earnings and profits (other than earnings and profits of the taxable year) in stock of the corporation (see line 34, below)				
25 percent of new capital				
Increase on account of intercorporate liquidation under section 761 (d) (2)				
Deficit in earnings and profits of another corporation under section 718 (a) (7)				
Total additions in lines 15 to 20				
Total of lines 14 and 21		\$	281,014	43
Average Reduction in Equity Invested Capital During the Taxable Year (See instructions for Schedule C, lines 1 to 12, included)				
Distributions not out of earnings and profits of the taxable year		\$		
Stock distributions from accumulated earnings and profits at beginning of year (see line 17, above)				
Decrease on account of intercorporate liquidation under section 761 (d) (3)				
Deficit in earnings and profits included in invested capital of another corporation (section 718 (b) (5))				
Total reductions in lines 23 to 26				
(See instructions for Schedule C, lines 15 to 21, included)				
Average equity invested capital (line 22 minus line 27)		\$	281,014	43
Average borrowed capital (attach schedule)		\$		
Average borrowed invested capital (50 percent of line 29)				
Average invested capital (line 28 plus line 30)		\$	281,014	43
Total inadmissible assets		\$		
Total admissible and inadmissible assets		\$		
Percentage which line 32 is of line 33				%
Reduction on account of inadmissible assets (..... percent of line 31)				
Invested capital (line 31 minus line 34)		\$	281,014	43
Portion of line 35 (not in excess of \$5,000,000); and credit at 8 percent		\$	22,481	15
Portion of line 36 (over \$5,000,000, but not over \$10,000,000); and credit at 7 percent				7%
Portion of line 36 (over \$10,000,000, but not over \$200,000,000); and credit at 6 percent				6%
Portion of line 36 (over \$200,000,000); and credit at 5 percent				5%
Excess profits credit—based on invested capital (total of lines 37 to 40)		\$	22,481	15

EXHIBIT J

Grace Bros. Inc.
Santa Rosa, Cal.

March 29, 1943

Garrett & Company, Inc.

Brooklyn

New York

Gentlemen:

We wish to advise you that, according to our agreement of January 20, 1943, the inventory as taken by Federal Inspector Pedersen on January 20, 1943, is as follows:

248,635 Gallons Dry Wine

274,126 Gallons Sweet Wine

The above to be paid for at the rate of 50c per gallon.

Included in this inventory, however, is five tanks containing 73,628 gallons of sweet wine which contains sugar above the standard, and which is to be paid for at 4c per gallon additional.

Very truly yours,

DE TURK WINERY,

By /s/ MANUEL FELCIANO,
Atty-in-fact.

MF:1mc [159]

EXHIBIT L

From Garrett & Co.
Cucamonga, Calif.

June 18, 1943

Mr. Joseph T. Grace,
c/o DeTurk Winery,
Santa Rosa, Calif.

Dear Mr. Grace:

On May 26th we wrote you, as per attached copy, requesting that you render billing to our Brooklyn office for the gallonage of wines as finally agreed upon between us.

On the date of June 14th they advised that they have not received this and are very anxious to have it immediately, before closing their books toward the end of this month, so will you please attend to this promptly and let us have a copy here for our records and greatly oblige.

Very truly yours,

GARRETT & CO., INC.,

L. A. WELLER,
Vice President.

LAW:cp Encl. [161]

EXHIBIT M

L. A. Weller

November 5, 1946

J. Campbell Moore

Dear Campbell:

I have just had a visit from a Mr. McFarland and Mr. Tonjes, the former from the San Francisco office and the latter from the Los Angeles office of the Internal Revenue Department. It seems that they have a tax suit against Mr. Grace over our deal with him for the Santa Rosa wine and plant lease and they asked for my version of the transaction.

They read me Mr. Grace's statement of the transaction which was all right with two exceptions and one was that Mr. Grace claims that when we were dickering he wanted to sell us the winery and made a price of \$125,000.00 on it but that we insisted that we would prefer a lease. I find nothing in the exchange of our telegrams about his wanting to sell us the plant or do I have any recollection of it and just what bearing this angle has on this case I don't quite understand. Another mis-statement was that it was I who put them in touch with the Taylor Company who bought the plant in early 1944. The fact is that I didn't know who Mr. Grace was dickering with until the deal was practically closed.

In going through my file here they were interested to know the exact amount of wine involved and we found this checked with the statement that Mr. Grace had made to them but one thing that interested them was that in one of Mr. Grace's wires to us, of which I have copies of course, he went on

to recite the gallonage of wine he was offering and mentioned the price of 40c on some dry red and 55c on some dry white and 65c on the sweets. They asked me why we finally decided on the flat price of 50c all the way through and I told him it was simply to simplify the transaction and I felt pretty sure the check would show that at the prices mentioned above for the various quantities involved it would average about 50c. In this telegram of Mr. Grace's dated December 29, 1942 he mentions \$12,000.00 as his lease price per year and they wondered why this was changed so I told them that we simply told Mr. Grace that \$12,000.00 was excessive and finally agreed on \$10,000.00 a year.

They were quite curious to know how this price of \$125,000.00 had got into the deal as the purchase price and I was able to [162] find a letter to Rossi Brothers written while we were trying to get out from under our lease when they had asked me to get a price from Mr. Grace on the winery because they were not on friendly terms with him and over the phone at that time Mr. Grace mentioned the \$125,000.00. My letter shows that in this conference with Mr. Grace he asked if I was asking for a price for ourselves and I explained to him that we were not interested in purchasing and that it was for another party who had asked me to get a price for them. When I told Mr. Rossi about this he thought the price excessive and dropped the matter and Mr. Grace later sold to Taylor for \$150,000.00 but I am quite sure that at the time that we made this deal with Mr. Grace in late December of 1942, the ques-

tion of the purchase of the winery was not brought up at all.

I think one thing these fellows had in mind too was whether or not the price of this lease was excessive from our standpoint and whether or not we agreed to this simply to get this wine and so I told them we did not consider \$10,000.00 excessive but that it was a part of Mr. Grace's stipulation for the sale of wine, that he would not sell the wine unless we took a lease on the plant—that we had long wanted a plant in that district anyway so had no objection to making a lease and considered \$10,000.00 a year reasonable. These two gentlemen were very courteous and agreeable and wanted me to give them copies of these telegrams, to and from Mr. Grace, and also a copy of the wine inventory so I told them I felt a hesitancy in doing this unless with the approval of the Brooklyn office and so he is writing you and Paulie today to authorize me to give them copies.

I can see no harm in this and don't know why we should hesitate to do this and I am afraid if we don't they may sub-peona me to produce these wires and correspondence and I would sure hate to get involved in a long drawn out hearing which is to be held soon in San Francisco. They told me quite frankly that they might wish me as a witness in any event but that they would see if they could arrange to have my deposition taken instead of my having to appear as a witness, so unless there are objections that I don't see I wish you would wire them or me to let them have copies of these wires

and letters showing the discussions and results of this deal. I find that they had a copy of our original agreement with Mr. Grace dated January 20, 1943 and also a copy of the final lease.

Awaiting your reaction by wire and hoping to see you out here soon, I am,

Sincerely yours,

L. A. WELLER.

LAW:mw

[Endorsed]: Filed May 25, 1947.

[Title of Tax Court and Cause.]

DESIGNATION OF CONTENTS OF RECORD
ON APPEAL

To the Clerk of The Tax Court of the United
States:

You are hereby requested to prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, copies duly certified as correct, of the following documents and records in the above-entitled cause in connection with the Petition for Review by the United States Circuit Court of Appeals for the Ninth Circuit heretofore filed by the above-named petitioner.

1. Docket entries.
2. Pleadings.

(a) Amended petition and notice of deficiency attached to the original petition as Exhibit A and referred to in the amended petition.

(b) Answer of respondent to the amended petition. [164]

3. Findings of Fact and Opinion of The Tax Court of the United States.

4. Decision of The Tax Court of the United States.

5. Petition for Review.

6. Notice of Filing Petition for Review.

7. Statement of Points to be Relied Upon on Appeal.

8. Statement of Evidence.

9. The Stipulation of Facts with the exhibits attached thereto.

10. The following exhibits introduced in evidence at the time of the hearing before The Tax Court:

(a) Respondent's Exhibit F—The final corporation income and declared value excess profits tax return of Grace Bros., Inc., for the year 1943.

(b) Respondent's Exhibit H—The final excess profits tax return of Grace Bros., Inc., for the year 1943.

(c) Respondent's Exhibit I—Consisting of nine telegrams.

(d) Respondent's Exhibit J—A letter dated Mar. 29, 1943, addressed to Garrett and Company by the DeTurk Winery by Manuel Felciano, attorney in fact.

(e) Respondent's Exhibit K—A letter dated May 26, 1943, addressed to Joseph T. Grace by L. A. Weller.

(f) Respondent's Exhibit L—A letter dated June

18, 1943, addressed to Joseph T. Grace by Garrett and Company.

(g) Respondent's Exhibit M—An inter-office letter dated November 5, 1946, from L. A. Weller to J Campbell Moore of Garrett and Company. [165]

11. This Designation of Contents of Record on Appeal.

/s/ GEORGE H. KOSTER,
/s/ BAYLEY KOHLMEIER,
Attorneys for Petitioner.

Agreed to June 24, 1948.

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of
Internal Revenue.

(Affidavit of Service by Mail attached.)

[Endorsed]: Filed June 21, 1948. [166]

[Title of Tax Court and Cause.]

CERTIFICATE

I, Victor S. Mersch, clerk of The Tax Court of the United States, do hereby certify that the foregoing pages, 1 to 166, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 2nd day of July, 1948.

(Seal) /s/ VICTOR S. MERSCH,
Clerk, The Tax Court of the
United States.

[Endorsed]: No. 11976. United States Court of Appeals for the Ninth Circuit. Grace Bros., Inc., Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review a Decision of The Tax Court of the United States.

Filed July 16, 1948.

 /s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the
Ninth Circuit.

United States Court of Appeals
for the Ninth Circuit

Docket No. 11976

GRACE BROS., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.STATEMENT OF POINTS TO BE RELIED
UPON ON APPEAL AND DESIGNATION
OF PORTION OF RECORD TO BE
PRINTED

Comes now the petitioner above named by its attorneys of record and states that it intends to rely on appeal upon all and each of the errors assigned in the Petition for Review herein, and petitioner formally adopts the errors assigned in said Petition for Review as its Statement of Points to be Relied Upon on Appeal.

Petitioner further states that the portions of the record designated for omission from the printed transcript in the Stipulation of Portion of Record to be Printed, filed herein, are not necessary for the consideration of the issues presented on appeal and requests that the entire record except the portions thereof designated for omission therefrom in said Stipulation of Portion of Record to be Printed, be included in the printed transcript. Petitioner further requests that said Stipulation of Portion

of Record to be Printed and this Statement of Points to be Relied Upon and Designation of Portion of Record to be Printed be included in the printed transcript.

Dated August 18, 1948.

Respectfully submitted,

/s/ GEORGE H. KOSTER,

/s/ BAYLEY KOHLMEIER,

Attorneys for Petitioner on
Review.

(Affidavit of Service by Mail attached.)

[Endorsed]: Filed August 20, 1948. Paul P.
O'Brien, Clerk.

[Title of U. S. Court of Appeals and Cause.]

STIPULATION OF PORTION OF RECORD
TO BE PRINTED

It is hereby stipulated and agreed by and between the parties hereto through their respective counsel of record that the portions of the record designated below are not necessary for the consideration of the issues presented on appeal and the clerk of the Court is requested to omit the following portions of the record from the printed transcript.

1. Pages 18 to 33, inclusive, of the certified record, being pages 5 to 15, inclusive, of the deficiency notice (Exhibit A attached to the Petition) and Exhibits A, A-1, B, B-1 and C attached to said deficiency notice.

2. Pages 133 and 134 of the certified record, being the California Franchise Tax Return for the year 1943 attached to the Stipulation of Facts as Exhibit 5-E.

3. Pages 141, 142 and 143 of the certified record, being letters and statements with regard to the extension of time for filing Petitioner's Income and Declared Value Excess Profits Tax Return (Form 1120) for the year 1943 and comprising part of Respondent's Exhibit F.

4. Page 146 of the certified record, being Schedule B of Petitioner's Excess Profits Tax Return (Form 1121) for the year 1943 and part of Respondent's Exhibit H.

5. Page 148 of the certified record, being a letter extending the time for filing Petitioner's Excess

Profits Tax Return (Form 1121) for the year 1943 and part of Respondent's Exhibit H.

6. Pages 149 to 158, inclusive, of the certified record, being nine telegrams comprising Respondent's Exhibit I, all of which were read into the record and are reproduced in full on pages 27 to 31 of the Statement of Evidence and on pages 88 to 92 of the certified record.

All of the certified record not designated herein for omission shall be printed.

Dated this 17th day of August, 1948.

Respectfully submitted,

/s/ GEORGE H. KOSTER,
/s/ BAYLEY KOHLMEIER,
Attorneys for Petitioner.

/s/ THERON LAMAR CAUDLE,
Assistant Attorney General,
Attorney for Respondent.

[Endorsed]: Filed August 20, 1948. Paul P. O'Brien, Clerk.



No. 11,976
IN THE
United States Court of Appeals
For the Ninth Circuit

GRACE BROS., INC.,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

Respondent.

PETITIONER'S OPENING BRIEF.

GEORGE H. KOSTER,

BAYLEY KOHLMEIER,

300 Montgomery Street, San Francisco 4, California,

Attorneys for Petitioner.

FILE

OCT 22 1948

PAUL P. O'BRIEN,
CLERK



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No. 11,976

IN THE

**United States Court of Appeals
For the Ninth Circuit**

GRACE BROS., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONER'S OPENING BRIEF.

JURISDICTIONAL STATEMENT.

This is an appeal from a decision of The Tax Court of the United States in which a deficiency in excess profits taxes was determined against petitioner for the year 1943. The findings of fact and opinion below are reported in 10 T. C. 158 and are set forth in full in the record herein. (R. 18.)

Petitioner is a California corporation which maintains its principal place of business in Santa Rosa, California. (R. 104.) Petitioner's income and excess profits tax returns for the year 1943 were duly filed with the Collector of Internal Revenue for the First District of California at San Francisco, California. (R. 4, 17.) Respondent determined a deficiency in petitioner's excess profits tax for the year 1943 in the

amount of \$114,190.49 and on September 20, 1945, pursuant to Section 272 of the Internal Revenue Code, respondent sent to petitioner a notice of said deficiency. (R. 10.) On December 10, 1945, pursuant to Section 272 of the Internal Revenue Code, petitioner filed its appeal to The Tax Court of The United States from said deficiency determination and thereafter on February 24, 1947 filed an amended petition to The Tax Court of the United States and alleged therein that it had overpaid its excess profits taxes for the year 1943 by the amount of \$23,913.11. (R. 4.) On March 19, 1947 respondent filed his answer to said amended petition, denying the claims and allegations of petitioner. (R. 16.) The appeal was called for hearing on May 26, 1947 and documentary and oral evidence was introduced by both parties. On January 27, 1948 The Tax Court of the United States promulgated its findings of fact and opinion (R. 18) and on April 5, 1948 the decision of the Tax Court was entered, determining a deficiency in petitioner's excess profits taxes for the year 1943 in the amount of \$124,073.01. (R. 31.)

On June 14, 1948, under authority of Section 1141 of the Internal Revenue Code (Title 26, U. S. Code, Section 1141, as amended by Section 504 of the Revenue Act of 1942), petitioner filed its petition for review by this Court of said decision of The Tax Court of the United States. (R. 32.) This appeal and the transcript of record herein were duly filed and docketed in this Court on July 16, 1948. (R. 141.)

STATEMENT OF THE CASE.

The controversy herein involves petitioner's correct excess profits tax liability for the year 1943, which in turn depends upon the determination of the following general issue: Whether the gain or any part thereof realized by petitioner in 1943 from the sale of its inventory of wine and its winery business is long term capital gain or ordinary income subject to excess profits tax.

Petitioner is a California corporation which was organized in 1910 and which maintains its principal place of business in Santa Rosa, California, (R. 104.) In 1943 and for many years prior thereto petitioner was engaged in various business enterprises including farming, cattle raising, manufacturing and selling ice, cold storage, and manufacturing and selling beer. (R. 104.) In 1921 petitioner acquired the DeTurk Winery in Santa Rosa, California and from 1921 until 1942 was engaged, in addition to its other activities, in the business of manufacturing and selling wine under the trade name of the DeTurk Winery. (R. 104.) The DeTurk Winery had been built in 1876 and had been continuously operated at the same location by petitioner and the prior owner from 1876 until the end of 1942. (R. 50.) The wine produced and sold under the name of the DeTurk Winery was of better than average quality and enjoyed a good reputation. (R. 20, 43.) The operating staff of the winery also included valuable and well trained men. (R. 24, 57.) During the period from 1936 to 1942, inclusive, petitioner realized net profits from its winery business

ranging from \$7,995.20 to \$33,184.93. Petitioner's net profit from said winery business during the year 1942 was \$18,959.53. (R. 21.) During the year 1941 petitioner sold 157,518 gallons of dry wine in bulk and 8,888 gallons in bottles at an average price of 22.6¢ per gallon, and sold 46,943 gallons of sweet wine in bulk and 12,443 gallons in bottles at an average price of 37.2¢ per gallon. In 1942 petitioner sold 114,046 gallons of dry wine in bulk and 7,028 gallons in bottles at an average price of 22.2¢ per gallon, and 46,009 gallons of sweet wine in bulk and 10,268 gallons in bottles at an average price of 36.8¢ per gallon. As dry wine should be held for two years or more and red wine for one year for aging, petitioner kept a substantial inventory in stock. (R. 21.)

Some time prior to October, 1942 petitioner decided to go out of the winery business and to dispose of the DeTurk Winery. (R. 52.) As the result of this decision petitioner limited its production of wine in the 1942 vintage season to 4,959 gallons which it extracted from grapes grown by it, whereas normally petitioner's annual production was approximately 200,000 gallons. (R. 21.)

Mr. Joseph T. Grace, the president and sole stockholder of petitioner, was actively in charge of petitioner's business affairs. In November, 1942, Mr. Grace advised Mr. L. A. Weller, vice president of Garrett and Company, Inc. of New York, that petitioner intended to discontinue the wine business and carried on negotiations and correspondence with Garrett and Company through Mr. Weller with regard to

the sale of the wine and winery business of petitioner to Garrett & Co. (R. 21, 53.) Mr. Grace advised Mr. Weller that petitioner would not sell its wine inventory unless it sold everything connected with its wine business, including the winery and the good will. (R. 53.) At that time petitioner had an inventory of 522,761 gallons of wine and Mr. Grace advised Mr. Weller that the winery was worth \$125,000 and the inventory and good will were worth \$250,000. (R. 104, 54.) Mr. Grace based his valuation of \$250,000 for the wine and the good will by estimating that petitioner could realize \$150,000 from the wine by continuing to sell it in the regular course of business and by estimating the value of the good will at five times the average annual net earnings of the wine business, making a good will value of \$100,000. (R. 54-55.)

After numerous conversations and telegrams between Mr. Grace and Mr. Weller and other officers of Garrett and Co., on December 31, 1942 Garrett and Company offered to lease petitioner's winery and equipment for five years at an annual rental of \$10,000 and to purchase all of petitioner's wine at 50¢ per gallon (R. 55-56, 70-75). Since the amount to be paid by Garrett & Co. on this basis gave to petitioner the full amount it was asking for its wine and its winery business, petitioner accepted the offer and shipped 104,000 gallons of wine that day. Petitioner received \$52,000 for the first shipment of wine and reported the income in its 1942 income tax return (R. 22.) Petitioner and Garrett & Co. entered into a written agreement, dated January 20, 1943, with regard to the trans-

fer of the wine and the lease of the property (R. 105, 111-116). In 1943 petitioner transferred the balance of its wine, consisting of 248,635 gallons of dry wine and 170,126 gallons of sweet wine, its bottles and cooperage, its DeTurk labels, its customer list, and its winery personnel to Garrett & Co. (R. 23, 106.) Petitioner also delivered possession of its winery to Garrett & Co. and surrendered its permit to manufacture and sell wine so that Garrett & Co. could procure a permit to operate a winery on the premises (R. 24, 57-58). After the transfer of the above assets, neither petitioner nor Mr. Grace engaged in the making or selling of wines (R. 24). During the year 1943 Garrett & Co. paid to petitioner \$124,317.50, computed at 50¢ a gallon, for 248,635 gallons of dry wine, \$94,862.41 computed at 50¢ a gallon for 96,498 gallons of sweet wine, and a somewhat higher price per gallon for 73,628 gallons of sweet wine which contained a higher sugar content than was required by California standards (R. 23, 106). As the total price agreed upon was slightly greater than the price originally asked, Mr. Grace considered that petitioner had sold the entire business, including good will, to Garrett & Co. and that petitioner had received \$100,000 for the good will of the winery business (R. 54, 56).

In its income tax return and its excess profits tax return for 1943 petitioner treated the sale as a sale of capital assets held for more than six months and reported a long term capital gain in the amount of \$140,133.58, which gains are not subject to excess profits tax (R. 127). Respondent treated the gain

from the sale as ordinary business income and thereby substantially increased petitioner's net income subject to excess profits tax and substantially increased petitioner's excess profits tax liability for 1943 (R. 13).

In its appeal to the Tax Court petitioner presented the following contentions:

1. At least \$100,000 was received by petitioner for its good will which was unquestionably a capital asset and therefore at least \$100,000 of the gain was long term capital gain realized from the sale of the good will.

2. The transaction with Garrett & Co. involved the disposition of a unitary business as distinguished from particular assets, and therefore the entire profit from the transaction should be treated as long term capital gain and taxed accordingly.

3. When petitioner decided to discontinue making wine and to dispose of the winery business, the wine on hand ceased to be held for sale to customers in the ordinary course of petitioner's business, and became a capital asset, and having been held for more than six months (except the 4,959 gallons manufactured in 1942) the gain constituted long term capital gain.

The Tax Court disregarded the testimony of the witnesses and determined that the transaction between petitioner and Garrett & Co. was not a disposition of the business as a unit and further determined that since the winery was leased and not sold to Garrett & Co. and since the price was determined on the basis of 50 cents per gallon for the wine, the sale did not

cover anything but wine, that the wine was not converted into a capital asset and that no part of the consideration received by petitioner was received for good will or other intangible assets. The Tax Court affirmed the determination of respondent. (R. 25-30.)

SPECIFICATIONS OF ERROR.

In making and rendering its decision, as aforesaid, The Tax Court of the United States erred to the prejudice of petitioner in the following respects:

1. In determining a deficiency in petitioner's excess profits tax for the calendar year 1943 in the amount of \$124,073.01.

2. In failing to determine that there was no deficiency in excess profits tax due from petitioner for the year 1943 and that petitioner overpaid its excess profits tax for said year by the amount of at least \$23,913.11.

3. In determining that the stock of wine sold by petitioner during the year 1943 was not a capital asset and that the gain derived therefrom was ordinary income and not capital gain.

4. In determining that the transaction with Garrett & Co. did not involve the disposition of a unitary business, as distinguished from particular assets, the profit from which should be treated as long term capital gain.

5. In determining that no part of the consideration received by petitioner for its wine and other assets connected with its winery business

was received for the good will of said winery business.

6. In failing and refusing to determine that at least \$100,000 of the consideration received by petitioner for its wine and other assets connected with the winery was received by petitioner for the good will of petitioner's winery business.

7. In failing and refusing to accept the uncontradicted testimony of the president of petitioner that the petitioner sold its good will and that the consideration received by petitioner upon the sale of its wine and other assets of its winery business exceeded the fair market value of the tangible assets sold by at least \$100,000 and that said \$100,000 represented consideration received by petitioner for the good will of its winery business.

SUMMARY OF ARGUMENT.

I. The evidence clearly establishes that in the transaction with Garrett & Co. it was petitioner's intention to sell its entire winery business including the good will of that business which petitioner valued at \$100,000, that petitioner advised Garrett & Co. that it would not sell any of the assets of its winery business unless it sold the entire business including the good will, that the selling price fixed by petitioner included \$100,000 for the good will, that Garrett & Co. offered and petitioner accepted a price, computed on the basis of fifty cents per gallon for the wine, which was slightly larger than the price asked by petitioner for the assets transferred, including the good will. As

petitioner received the full price it asked it considered that it received full consideration for its good will.

While the written communications between the parties were in the form of a sale of wine and a lease of the winery the evidence establishes that the transaction was intended to be and was in substance and effect, if not in form, a sale of the entire winery business including the good will.

The courts have recognized that a sale of a going business necessarily involves a sale of the good will of the business and have held that a portion of the price must be allocated to the good will.

The Tax Court erred in ignoring the uncontradicted testimony of a qualified witness and in refusing to consider the substance and effect of the entire transaction and its determination that the transaction did not involve a sale of good will was clearly erroneous and should be reversed.

II. As the transaction between petitioner and Garrett & Co. was a sale of the entire winery business as a going concern the gain realized therefrom was long term capital gain and the Tax Court erred as a matter of law in determining that the gain was ordinary income.

III. When petitioner determined to discontinue its winery business and to sell all the assets thereof the wine inventory ceased to be held primarily for sale to customers in the ordinary course of business and became a capital asset. The gain realized from the

sale of the wine, except the 4,959 gallons produced in 1942, constituted long term capital gain. The Tax Court erred as a matter of law in determining that the wine did not become a capital asset and that the gain from the sale thereof was ordinary income.

ARGUMENT.

I. INTRODUCTORY STATEMENT.

The issues presented to the Tax Court in the proceeding below and the issues presented to this Court in this appeal arise out of the sale by petitioner of the assets owned and used by it in the operation of its winery business prior to the sale. There is no controversy with regard to the cost or other basis of the assets sold, the total consideration received by petitioner upon the sale, or the total gain realized from the sale. The basic issue involved is whether all or any part of the gain realized by petitioner was capital gain or ordinary income. The determination of this basic issue depends upon the determination of the subordinate issues of (1) whether part of the consideration was received by petitioner for the good will of its business, (2) whether the transaction was a disposition of a unitary business as distinguished from particular assets, and (3) whether the wine involved was converted into a capital asset before the sale. The determination of *any* of the above issues in favor of petitioner will require the reversal of the decision of the Tax Court.

The determination of the above issues has an important effect for tax purposes for the reason that long term capital gains were not subject to the excess profits tax which was in effect for the year 1943, whereas ordinary income was subject to the excess profits tax.

Petitioner's interpretation of the transaction is that it was a sale of its entire winery business, including the good will, and not a mere sale of its stock of wines as determined by respondent and the Tax Court. Petitioner contends that at least \$100,000 of the consideration received by it for the business and assets was received for good will and constituted capital gain. Petitioner further contends that its decision to discontinue the operation of the winery business and to sell all of the assets thereof effected a conversion of the wine held in inventory to a capital asset and that the gain realized upon the subsequent sale of the business and assets was capital gain.

Under petitioner's interpretation of the transaction the entire profit realized was capital gain and petitioner reported the gain accordingly in its income tax return. Respondent determined that the transaction involved only a sale of wine and that the entire gain was ordinary income. The Tax Court sustained respondent's determination.

The above issues are mixed questions of law and fact which involve the legal effect and the proper legal interpretation of the facts established by the evidence in the case. Petitioner does not challenge any

of the facts specifically found by the Tax Court in its Findings of Fact. However, in its opinion the Tax Court states that it is unable to find certain facts which petitioner contends are clearly established by the evidence. The statements in the opinion of the Tax Court were not made as findings of fact, but merely as comments on the evidence and should not be accepted as findings by the Court. *Kelleher v. Commissioner* (CCA-9, 1938) 94 F (2d) 294; *Aronson v. Commissioner* (CCA-9, 1938) 98 F (2d) 23; *Belridge Oil Company v. Helvering* (CCA-9, 1934) 69 F (2d) 432. But even if the statements, which will be specifically discussed in the following portions of this brief, can be considered as findings of fact, it is petitioner's contention that the inferences and conclusions of the Tax Court are not supported by any substantial evidence, are contrary to the uncontradicted testimony of the witnesses and other competent evidence in the record and are clearly erroneous.

This Court has full power and jurisdiction to review the findings and conclusions and decision of the Tax Court and is no longer restricted by the doctrine of *Dobson v. Commissioner* 320 U. S. 489, 64 S. Ct. 239, 88 L. Ed. 248. Section 1141(a) of the Internal Revenue Code, as amended by Section 36 of Public Law 773, 80th Congress, Second Session, which became effective on September 1, 1948 provides:

“The Circuit Courts of Appeals and the United States Court of Appeals for the District of Columbia shall have exclusive jurisdiction to review the decisions of the Tax Court, except as

provided in Section 1254 of Title 28 of the United States Code, *in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury; * * **” (Italics supplied.)

Appellate courts have full power to review conclusions of law of the trial Court and also have power to review findings of fact subject to the limitation contained in Rule 52(a) of the Rules of Civil Procedure for the District Courts of the United States which provides “* * * Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial Court to judge of the credibility of the witnesses”. While, under the above rule, the appellate courts have refused to set aside pure findings of fact of the trial Court, supported by substantial evidence, the courts have generally held that appellate courts have full power to review and set aside findings which are based upon a misapplication of misinterpretation of the law to the evidentiary findings and are not bound by the trial Courts’ inferences and conclusions drawn from undisputed evidentiary facts.

Kuhn v. Princess Lida of Thurn & Taxis, 3 Cir., 1941, 119 F (2d) 704; *Compana Corp. v. Harrison*, 7 Cir., 1940, 114 F (2d) 400; *United States v. Armature Rewinding Co.*, 8 Cir., 1942, 124 F (2d) 589.

In the recent decision of *United States v. United States Gypsum Co.*, 1948, 333 U. S. 364, 92 L Ed (Ad. Op.) 552, 68 S. Ct. 525, the United States Supreme Court set aside numerous findings of fact of the dis-

strict Court after a careful and extensive review of the evidence on the ground that the findings were clearly erroneous. The Supreme Court defined the meaning of "clearly erroneous" as used in Rule 52(a) (supra) as follows:

"A finding is 'clearly erroneous' when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." (Italics supplied.)

As stated above petitioner is not challenging the facts set forth in the Tax Court's findings of fact but does contend that the ultimate conclusions of the Tax Court are clearly erroneous, are based upon inferences and interpretations of the evidence which are not supported or justified by the facts and upon misinterpretations of applicable principles of law. This Court has full power to review conclusions of law of the Tax Court and under the law as amended and the above cited decisions has power to review findings of fact and may set aside findings of fact as clearly erroneous if upon the entire evidence the Court is of the definite and firm conviction that the Tax Court committed a mistake.

II. AT LEAST \$100,000 OF THE CONSIDERATION RECEIVED BY PETITIONER FOR THE ASSETS OF ITS WINERY BUSINESS WAS RECEIVED BY PETITIONER FOR THE GOOD WILL OF ITS SAID BUSINESS AND CONSTITUTED CAPITAL GAIN.

(a) Summary of pertinent facts.

One of the questions presented to and decided by the Tax Court was whether any part of the consideration received by petitioner upon the sale of the assets of its winery business was received for the good will of said business. In its opinion (R. 27), the Tax Court stated that it was unable to find that petitioner sold anything not covered by the sale contract (Stip. of Facts, Ex. 2-B) (R. 111). In order that petitioner's contentions with regard to this issue may be clearly understood it is necessary to summarize the facts.

In 1942 and prior thereto petitioner was engaged in various business enterprises including farming, cattle raising, manufacture and sale of ice, cold storage, manufacture and sale of beer and the manufacture and sale of wine. (R. 20, 104.) Petitioner entered the wine business in 1921 when it acquired the DeTurk Winery which had been constructed in 1876 and had been continuously operated under that name at the same location. Petitioner continued in the wine business under the name of DeTurk Winery until the end of 1942 and operated said business as a separate enterprise from its other operations. (R. 104.) The wine produced and sold by petitioner under the name of the DeTurk Winery was of better than average quality and enjoyed a good reputation. (R. 20, 43.)

Likewise the operation of the winery was successful and produced a good income. (R. 21, 121.)

Sometime prior to October, 1942, petitioner decided to go out of the wine business and reduced its wine production in 1942 from a normal 200,000 gallons to 4959 gallons which it extracted entirely from grapes grown by it. (R. 21, 105.) Mr. Joseph T. Grace, who was the sole stockholder, president and active manager of petitioner's business affairs talked to different people about the sale of the wine business and in November, 1942, he advised Mr. L. A. Weller, vice-president of Garrett & Co., Inc., of New York, that petitioner intended to dispose of its wine business. Mr. Grace advised Mr. Weller that the winery was worth \$125,000 and that the inventory and good will were worth \$250,000, making a total of \$375,000 for everything. In determining that the wine inventory and good will were worth \$250,000 Mr. Grace estimated that the wine could be sold at current prices for approximately \$150,000 and he valued the good will at \$100,000. (R. 54.)

At another meeting shortly thereafter Mr. Weller inquired as to whether petitioner would lease its winery and stated, "*I can give you what you ask for your wine inventory and everything that goes with it, the good will, which would be equivalent to \$250,000. * * * If I give you fifty cents a gallon, that will give you what you are asking.*" (R. 56.)

Thereafter there were a series of telegrams and conversations between the parties which referred pri-

marily to wine and which finally resulted in an agreement which provided for the sale of petitioner's wine (approximately 520,000 gallons at fifty cents per gallon plus a small additional amount for wine which had a higher sugar content than that required by California standards), and the lease of the winery and equipment for a term of five years with the right of renewal at an annual rental of \$10,000 per year. On December 31, 1942, petitioner delivered 104,000 gallons of wine and received \$54,000 therefor. In 1943 petitioner delivered the remaining 418,761 gallons of wine and received \$219,179.91. Petitioner also transferred to Garrett & Co. its wine stocks, its cooperage, its labels, its list of customers and its staff of eight or ten experienced employees and surrendered its permit to manufacture and sell wine so that Garrett & Co. could procure a permit to operate on the premises. Thereafter neither petitioner nor Mr. Grace engaged in making or selling wine. (R. 22-24.)

The record in this case leaves no room for doubt that the winery business of petitioner, which was separately operated under the name of DeTurk Winery, possessed good will which had a substantial value. The good reputation of the product, the earnings of the business and the testimony of qualified witnesses all establish that fact. Mr. Morrow, who had been engaged in the wine business for fifty-five years and who was thoroughly familiar with petitioner's wine and business, testified that petitioner's wine business had a substantial going concern or good will value. (R. 44, 45.) Mr. Grace, the president and active man-

ager of petitioner, valued the good will of petitioner's wine business at \$100,000 (R. 55, 60) and Mr. Tapp, an experienced banker, with extensive experience in and knowledge of the wine business, testified that a business such as that of the DeTurk Winery would have a good will value of approximately \$160,000. (R. 99.) There is also a legal presumption that a profitable business has a good will or going concern value over and above the value of the tangible assets. *Pflegghar Hardware Specialty Co. v. Blair*, 2 Cir., 1929, 30 F (2d) 614; *Helvering v. Security Savings and Commercial Bank*, 4 Cir., 1934, 72 F (2d) 874; *White and Wells Co. v. Commissioner*, 19 BTA 416; *Wyman and Co. v. Commissioner*, 8 BTA 408. See also *Randolph Paul, Federal Estate and Gift Taxation*, Vol. 2, p. 1242.

The Tax Court did not question the fact that there was a substantial good will value in petitioner's winery business, but based its decision upon the determination that the transaction between petitioner and Garrett & Company did not involve the sale of petitioner's good will and that the entire consideration received by petitioner was paid to it for the wine inventory. The petitioner contends that the determination of the Tax Court that no part of the consideration received by petitioner was received by it for its good will or going concern value is not supported by the evidence in the record or the applicable principles of law.

(b) The evidence establishes that petitioner intended to and actually did sell its good will.

The uncontradicted testimony of Mr. Grace, who represented petitioner in the negotiations, was that petitioner would not sell its wine inventory except as a part of the sale of all the assets of the winery business, including the good will which he valued at \$100,000, and he so advised the purchaser. (R. 53, 54.) The purchaser offered to lease the winery instead of purchasing it and offered to purchase the wine at a price which would give petitioner an amount equal to the price at which the wine, the good will and the other assets had been included in petitioner's original offer. (R. 56.) Thereafter, the telegrams which passed between the parties and the final letter which evidenced the agreement referred only to the wine and established the total consideration on the basis of the wine transferred. The evidence clearly establishes, however, that despite the wording of the telegrams and the agreement letter, petitioner actually transferred and delivered to Garrett & Co. by sale and lease, not only wine, but also all the other assets of its wine business, including its labels and list of customers, transferred its staff of experienced employees to Garrett & Co. and surrendered its permit to manufacture and sell wine so that Garrett & Co. could procure a permit to operate on the premises.

Upon the completion of the transaction Garrett & Co. owned all of the assets, tangible and intangible, which petitioner had formerly owned and used in its wine business, except the winery and equipment, and

Garrett & Co. had a five year lease of the plant and equipment with the right of renewal. The above facts are not disputed and were found by the Tax Court. These undisputed facts clearly establish that despite the form of the transaction and the phraseology of the telegrams, the effect of the transaction was the transfer of the entire wine business and all of the assets thereof to Garrett & Co. The uncontradicted testimony of Mr. Grace also clearly establishes that it was the intention and understanding of petitioner that all of the assets, including the good will, were being sold and that the sale would not have been made on any other terms. (R. 53, 56.)

In its opinion the Tax Court specifically refers to the testimony of Mr. Grace with regard to the terms of the offer of sale which included \$100,000 for petitioner's good will but concluded, "We cannot find such an offer upon the evidence adduced." (R. 25.) The refusal of the Tax Court to give any weight or consideration to the uncontradicted testimony of Mr. Grace constituted reversible error. *Foran v. Commissioner*, 5 Cir., 1948, 165 F (2d) 409; *Tatt v. Commissioner*, 5 Cir., 1948, 166 F (2d) 697.

Furthermore, the consideration received by petitioner, while technically computed on the basis of the wine transferred, was approximately the amount which petitioner requested for all of the assets which it sold, including its good will, and exceeded the price asked for the wine by more than \$100,000. After the conclusion of the transaction petitioner had surrendered its permit to manufacture and sell wine and

had retained no part of the wine business or the assets thereof, except title to the winery and equipment which had been leased for five years, with right of renewal. By the transfers petitioner completely disposed of the good will of its winery business and the only logical and fair conclusion from all the evidence is that a portion of the consideration was received by petitioner for its good will.

(c) Applicable decisions establish a legal presumption that petitioner sold its good will when it sold its business.

The above conclusion is further supported by Court decisions which hold that the sale of a going business necessarily involves a sale of the good will of the business even though the good will is not specifically transferred or even mentioned in the contract between the parties. *White & Wells Co. v. Commissioner*, 19 BTA 416, 2 Cir., 1931, 50 F. (2d) 120; *Pflegghar Hardware Specialty Co. v. Blair*, 2 Cir., 1929, 30 F. (2d) 614; *Betts v. United States*, 62 Ct. Cls. 1.

In *Didlake v. Roden Grocery Co.*, 160 Ala. 484, 495, 49 So. 384, 387, the Court stated:

“* * * But the authorities are clear to the effect that, if a business is sold out entirely and nothing is said about good will, it goes with the property. This necessarily results from the fact that the good will cannot exist except in connection with the business.”

White & Wells Co. v. Commissioner (supra) and *Pflegghar Hardware Specialty Co. v. Blair* (supra) are almost identical in all material respects with the present case and in each of said cases it was held that

there was a sale of the good will of the business even though the contract of sale made no mention of good will and the transactions were in form mere sales of tangible assets.

White & Wells Co. v. Commissioner (supra) is exactly in point, and because this case seems undistinguishable and appears to be uncontrovertible authority to support a decision in favor of this petitioner, a review of that case follows:

White & Wells Co. operated two factories manufacturing paper boxes. The boxes manufactured in one of the factories were sold almost exclusively to two rubber companies. After a number of years, White & Wells Co. decided to sell this factory and finally did sell it to one of the rubber companies. It was not the intention of the rubber company to go into the paper box business or sell boxes to the public, but merely to manufacture them for use in its own business. The contract of sale entered into between White & Wells Co. and the rubber company specified only the sale of the land, buildings and equipment. The taxpayer contended that when it sold the factory, it sold a going business to which there was attached certain good will value and it should therefore be allowed to set up as part of the cost basis a March 1, 1913, value for the good will in determining the profit or loss from the sale. The Government contended that the good will was not sold and in the alternative objected to the taxpayer's computation of the good will value. The Board states the Commissioner's contentions as follows:

“In this proceeding, the respondent attempts to differentiate the *Pfleggar Hardware Specialty Co.* case from the instant case since in the former, the company sold its plant and went out of business, whereas, in the instant proceeding, the petitioner sold only one of its factories and continued in the general paper box business. It is further contended that the United States Rubber Co. did not buy the good will of the petitioner or of the Naugatuck Factory because the Naugatuck Factory was designed especially for manufacturing supplies for the rubber company; that it was not necessary for the rubber company to buy any good will of the plant.”

The Board after concluding that “*It is to be assumed that the manufacturer doing a profitable business will not sell his plant at any date for the residual value of its tangibles*” (italics supplied) determined that there was a disposition of intangible value in the transaction and that in computing profit from the sale of the factory, the March 1, 1913, value of the intangible assets should be considered as part of the basis. The final and concluding paragraph of the Board’s decision is significant in that it recognizes without question that even though the formality of the sale involved only the sale of the tangible property, there was, nevertheless, to be recognized as inherent in the transaction, a disposition of the intangible or going business value of the tangible property, and that final paragraph reads as follows:

“From a consideration of the entire record, we reach the conclusion that the going concern value of the petitioner’s Naugatuck Factory on March

1, 1913, was the amount of \$31,441.60, which amount added to the residual value of the tangibles of \$67,904.86, gives a basis for the determination of the profit upon the sale of the Naugatuck Factory of \$99,346.46. Since such factory was sold in 1920 for \$150,000 cash, the profit realized upon the sale was \$50,653.54.”

This case was appealed to the United States Circuit Court of Appeals for the Second Circuit, 50 Fed. (2d) 1209, and that Court agreed with the determination that the good will was sold but remanded the case back to the Board with instructions that in using earnings for an average period of years for the purpose of computing the value of the good will, the Board should include within the period certain years in which good earnings were realized in order that the period as a whole would reflect a fair average and measure for the valuing of the good will.

Just this recital of the *White & Wells Co.* case is sufficient to show its resemblance to present case. This case is even stronger in that there is ample evidence in the record that the petitioner intended to dispose of its intangible assets and included a price for those assets in the overall price which it quoted Garrett & Co. for the entire business and which it finally received in the transaction, and petitioner never re-engaged in the winery business.

In *Pfleggar Hardware Specialty Co. v. Blair* (supra) the Pfleggar company was engaged in the business of manufacturing and selling articles of hardware. It had one principal customer which pur-

chased 90% of its output and which sold the articles purchased under its own name and not under the name of Pflëghar. In 1919 the customer purchased Pflëghar Company's plant and equipment, exclusive of inventory, as a whole as a going concern for \$300,000. Pflëghar contended that it sold its good will and was entitled to include the March 1, 1913 value of the good will as a part of its cost in computing its profit on the sale. The Commissioner contended that there was no sale of good will in 1919 and that Pflëghar had no good will of value in 1913. The Board of Tax Appeals held for the Commissioner on the ground that while whatever intangible asset Pflëghar owned was transferred to the purchaser the evidence did not establish any value for good will in 1913. On appeal the Circuit Court for the Second Circuit reversed the decision of the Board of Tax Appeals on the grounds that the taxpayer had good will of value in 1913 and that since the subject of the sale was a manufacturing plant in production as a going concern the seller sold its good will.

In each of the cases discussed above the contracts of sale made no mention of good will, the good will of the seller was of no apparent value to the purchaser and the Commissioner contended, as in this case, that there was no sale of good will. The Courts held, however, that since the transactions involved the transfer of a going business the good will of the seller was included among the assets sold.

The principle of the above cases is directly applicable to the present case. As shown above petitioner

transferred its entire business as a going concern, including its staff of experienced employees, to Garrett & Co., retained no part of the business and thereafter completely ceased all operations in the wine business. Such a transfer of an entire business necessarily includes the transfer of the good will of the seller regardless of the terms of the contract of sale.

(d) The grounds and reasons relied upon by the Tax Court are not supported by the evidence and are contrary to the applicable principles of law.

The Tax Court based its decision herein primarily upon the fact that the telegrams between the parties did not suggest an intention to sell the winery, the fact that the winery was leased and not sold, the fact that the final price was computed on the basis of the wine transferred and the Court's belief that Garrett & Co. would not have paid \$100,000 for good will which the Court considered that it abandoned a little over a year later by canceling the lease. (R. 25-28.) None of the points relied upon by the Tax Court are sufficient to justify a determination that petitioner did not sell its good will or to distinguish *White & Wells Co. v. Commissioner* (supra) or *Pfleggar Hardware Specialties Co. v. Blair* (supra.)

The decision of the Tax Court also appears to be based to a large extent upon the assumption that there can be no sale of a business as a going concern or of the good will of a business unless the transaction includes the sale of the physical plant. The Tax Court clearly confused the business with the plant for the Court states "We should be impressed by this

argument (that there was a sale of a going business and such sale necessarily included a transfer of the good will) if there had been a sale as in the cited cases [*White & Wells Co. v. Commissioner* (supra) and *Pflegghar Hardware Specialties Co. v. Blair* (supra)], but under the facts here shown the advantages of what ever good will was inherent in petitioner's business passed to Garrett & Co. by lease, not by sale, * * *". (R. 26.) The basic assumption of the quoted statement, that there cannot be a sale of a going business unless the physical plant is sold is obviously fallacious. Good will is seldom inherent in a plant and equipment except possibly where location is the principal element of the good will. Likewise the abandonment or sale of the plant and equipment without a transfer of the business itself does not effect an abandonment or transfer of the good will of the business. *Wm. Wailes v. Commissioner*, 25 BTA 278.

There are many businesses with valuable good will which do not own the plant and equipment used and it is by no means unusual for one concern to buy the business and good will of another concern without buying or even leasing the physical plant and equipment of the seller. It so happened that in *White & Wells Co. v. Commissioner* (supra) and in *Pflegghar Hardware Specialties Co. v. Blair* (supra) the plants and equipment were sold, but that fact does not appear to have any important bearing upon the decisions in those cases.

In the present case there was much more than a mere sale of merchandise and a lease of the plant and equipment as stated by the Tax Court. Petitioner transferred its entire inventory of wines, its labels, its customer list, its employees, and it surrendered its permit to engage in the wine business and gave the purchaser a five year lease with right of renewal of the plant and equipment. Petitioner retained no part of its wine business and did not again engage in that business. Petitioner's intention to completely dispose of its wine business is corroborated by the fact that a year later it sold the plant and equipment and thereby disposed of the last interest it held in assets formerly used in the business. The leasing of petitioner's plant and equipment in connection with the sale and transfer of all the other assets was as effective for all practical purposes as a sale would have been and the fact that the plant was not sold does not make the rule of the above cited cases inapplicable, nor justify the conclusion that petitioner did not sell its entire business, including its good will.

The fact that the telegrams between the parties and the contract letter referred only to wine and the final price was based upon the quantity of wine transferred is of little importance when considered with all the evidence. Mr. Grace testified that he advised Mr. Weller that petitioner would not sell its wine except as a part of a sale of the entire business and all of the assets thereof, including the good will and he quoted a price of \$375,000 which consisted of \$125,000 for the plant and equipment, \$150,000

for the wine inventory, and \$100,000 for the good will. (R. 53-54.) Mr. Weller offered to lease the plant and stated that Garrett & Co. could give petitioner its price for the remaining assets by paying 50¢ per gallon for the wine. (R. 56.) As petitioner was willing to lease its plant in connection with the sale of the other assets of the business and the purchaser was willing to pay the price petitioner asked, the method employed in determining the price was obviously of no great importance to petitioner. Mr. Grace testified that he felt that petitioner was getting the price it was asking for the good will, the organization and all that. (R. 56.)

The conclusion that the transaction between petitioner and Garrett & Co. was merely a sale of wine can be reached only by ignoring all the evidence except the written communications and refusing to interpret the written documents in the light of the intention and understanding of the seller, the actual performance and the effect of the entire transaction. While the trial Court has broad powers in determining the facts of a case and interpreting the evidence, it cannot ignore competent evidence and base its determination upon a small portion of the evidence. *United States v. United States Gypsum Co.*, 1948, 333 U. S. 364, 92 L. Ed. (Ad. Op.) 552, 68 Sup. Ct. 525; *Fleming v. Palmer*, 3 Cir., 1941, 123 F. (2d) 749; *Belridge Oil Co. v. Commissioner*, 9 Cir., 1936, 85 F. (2d) 762.

The Tax Court also based its determination to a large extent upon its belief that Garrett & Co "would not have paid \$100,000 * * * to obtain good will which

it abandoned a little over a year later by canceling the lease* * *.” There is nothing whatsoever in the record to justify such belief, and the Tax Court has no power to substitute its judgment as to the sagacity of a business transaction for that of the parties. See *Belridge Oil Co. v. Commissioner* (supra). Furthermore, the mere abandonment of a plant in connection with the transfer of the business to another location does not constitute an abandonment of good will. *Wm. Wailes v. Commissioner*, 25 BTA 278.

The Tax Court’s belief in this regard was obviously influenced by its erroneous assumption that good will attaches to and is inseparable from the physical plant employed in the business.

While it may be that Garrett & Co. had no immediate need or desire for petitioner’s good will, the same could be said of the purchasers in *White & Wells Co. v. Commissioner* (supra) and *Pfleggar Hardware Specialties Co. v. Blair* (supra), and it does not follow that the good will was not sold and transferred along with the other assets. The record does clearly establish that petitioner intended and understood that its good will was being sold and would not have entered into the transaction on any other basis and that the purchaser was so advised. The record also establishes that the price paid was approximately the amount asked by petitioner for all the assets sold including its good will. We are here concerned with petitioner’s income and tax liability which must be determined on the basis of the assets which petitioner sold and transferred and not on the basis of

what the purchaser wanted or what it did with the assets after the purchase.

In the case of *Ida P. Huggins*, 1 T. C. 1214, P. H. T. C. Memo, Dec. Vol. 12, ¶ 43172, petitioner owned a piece of property improved with a building from which she was obtaining rentals. Sears Roebuck wanted the land for the erection of a retail store but had no use for the building. Sears Roebuck purchased the property for a lump sum payment and immediately demolished the building. The petitioner argued that since Sears Roebuck wanted only the land practically the entire sales price should be allocated as the selling price of the land, and only an amount equal to the junk value of the building should be allocated as the selling price of the building. Since the gain on the land was a capital gain and the loss on the building an ordinary loss the petitioner would have effected a tax saving if her contention had been sustained. The Tax Court in sustaining the Commissioner rejected her contention, and pointed out that in determining her tax liability the transaction must be analyzed from her point of view or from a reasonable construction of the transaction as it affected her regardless of the purposes or objectives intended by the other party to the transaction. The Tax Court pointed out that the building was an income producing assets and it was reasonable to assume that the petitioner would not have disposed of an income producing asset without receiving some consideration for it and the Court therefore allocated a fair portion of the selling price as the selling price

of the building regardless of the fact that Sears Roebuck from its point of view probably paid the entire price for the land alone.

In principle, the same situation exists in the instant case. It can be assumed for the moment that in the transaction here involved, Garrett & Co. was primarily interested in obtaining a stock of good wines and a going plant, as distinguished from a going manufacturing business. The sale of the wine alone would have meant the end of the DeTurk Winery business and the taxpayer indicated quite clearly that it wanted to sell its wine business and that it would not dispose of the wine without disposing of the entire winery business including the plant and the good will. The petitioner is contending here exactly what the Government contended in the *Ida P. Huggins* case, *supra*, namely, that insofar as the petitioner was concerned, it was disposing of one of its income producing assets, its good will or going concern value, and part of the selling price should be allocated to that asset. If the principle of the *Ida P. Huggins* case is sound it must be concluded that this petitioner would not have entered into a transaction involving the disposition of its wine business without receiving consideration for the good will thereof which was one of the income producing assets of substantial value *to the petitioner*, and therefore some part of the price received from Garrett & Co. should be allocated as being received for that asset, and it must be concluded further that this allocation

should be made regardless of how Garrett & Co. handled the transaction.

Petitioner submits that the principle of *Ida P. Huggins* (supra) is directly applicable to this case and that the issues presented must be determined by interpreting the transaction as it applied to petitioner without regard to what the purchaser may have wanted out of the transaction. Whether or not Garrett & Co. would have paid \$100,000 or anything at all for petitioner's good will as such is immaterial. The important fact is that petitioner would not have sold its business or assets piecemeal, insisted that its good will be purchased along with the other assets of the business and actually received the total price it asked for all of its assets, including its good will. When all the facts and circumstances are considered the only reasonable conclusion is that petitioner sold its entire wine business including its good will.

The opinion of the Tax Court clearly discloses that in reaching the conclusion that the transaction between petitioner and Garrett & Co. was merely a sale of wine and a lease of the plant and equipment the Court completely ignored the uncontradicted testimony of Mr. Grace as to the intention and understanding of petitioner, completely ignored the substance and effect of the transaction as a whole, completely disregarded the principle of *White & Wells Co. v. Commissioner* (supra) and *Pfleghar Hardware Specialties Co. v. Blair* (supra) and based

its conclusion entirely upon the form of the written documents and the erroneous assumption that there cannot be a sale of good will of a business without a sale and transfer of the physical plant and equipment. It is respectfully submitted that the Tax Court erred as a matter of law in disregarding the uncontradicted testimony of a competent and well qualified witness, in refusing to give any consideration and weight to the substance and effect of the entire transaction and in basing its conclusion entirely upon the form and wording of the written communications and the formal contract and upon inferences and assumptions not supported by the evidence or by established principles of law.

(e) The facts and evidence establish that at least \$100,000 of the consideration received should be allocated to the good will.

As the Tax Court concluded that the transaction between petitioner and Garrett & Co. did not include a sale of the good will it did not consider the allocation of the consideration received by petitioner between the good will and the assets sold. The record does contain facts and evidence from which a fair allocation of the consideration can be made.

Mr. Grace testified that at the inception of the negotiations he quoted to Mr. Weller a total price of \$375,000 which was composed of \$125,000 for the plant and equipment, \$150,000 for the wine inventory and \$100,000 for the good will (R. 54.) He further testified that he determined the value of the wine inventory at the price for which it could have been

sold in the regular course of business and determined the value of the good will at five times normal earnings (R. 60.) The elimination of the plant and equipment from the assets being sold reduced the total consideration asked to the \$250,000 asked for the wine and good will. The price finally agreed upon and received was \$271,179.91.

The Stipulation of Facts (par. 6, R. 104) shows that the average price at which the DeTurk Winery had been selling its wine in the year 1942 was 22.2¢ per gallon for dry wine and 36.8¢ per gallon for sweet wine. The wine involved in the sale to Garrett & Co. was 352,635 gallons of dry wine and 170,126 gallons of sweet wine. (R. 105.) By applying the average prices to the gallonage the amount which DeTurk Winery would have received would have been \$150,-891.34 almost the exact amount estimated by Mr. Grace.

The Tax Court attached significance to the fact that petitioner did not introduce evidence to show the market price of the wine in December, 1942. The purpose of the stipulation with regard to the average selling price of the wine in 1942 was to establish the market value of the wine and the price at which it could have been sold in the regular course of business. In agreeing to the stipulation of the average price at which the wine was sold in 1942 respondent was necessarily fully informed of the price at which wine was sold in December, 1942. If that price had been appreciably higher than the average price for the year there can be no doubt that respondent would

have introduced such fact in evidence. Also it is obvious that Mr. Grace was familiar with the price in December, 1942 and his estimate of the price is consistent with the average price for the year. The stipulated average price and respondent's failure to suggest that the price was higher in December, 1942 together with his failure to challenge Mr. Grace's estimate of the price at which the wine could have been sold in the regular course of business should satisfactorily establish that the value of the wine in December of 1942 was not appreciably greater than the average price for the year.

Mr. Grace's allocation of \$100,000 of the consideration to good will should be acceptable by the Court. There can be no doubt as to his qualification to place a value on the good will. He was experienced in the business and was the one who actually determined the price at which the assets would be sold. Furthermore, his valuation of the other principal assets, namely the wine at \$150,000 and the plant at \$125,000, are shown to be reasonable and accurate on the basis of actual sales. Mr. Grace's allocation is further corroborated by the testimony of Mr. Tapp who testified that the good will of the DeTurk Winery business was approximately \$160,000 (R. 99.)

Petitioner respectfully submits that the record contains ample evidence from which a fair allocation of a portion of the consideration to the good will can be made and that the evidence clearly shows that at least \$100,000 of the consideration should be allocated to the good will.

- (f) **The determination of the Tax Court that no part of the consideration received by petitioner was received for the good will of its winery business was clearly erroneous and should be reversed.**

The stipulated facts and other evidence presented to the Tax Court clearly establish that the winery business of petitioner had a substantial good will or going concern value. The evidence also establishes that in the transaction with Garrett & Co. petitioner sold and transferred its entire wine business and retained only the reversionary interest in its plant and equipment. The Courts have recognized that the transfer of a going business necessarily involves the transfer of the good will of the business and have held that as a matter of law such a sale involves the sale of the good will even though it is not mentioned in the contract and even though the purchaser may have no apparent need or desire for the good will. The Courts have also recognized that the seller would not part with its good will without receiving consideration therefor and have held that part of the consideration must be allocated to the good will even though the contract of sale bases the price entirely upon the tangible assets transferred.

In the present case, in addition to the foregoing factors, the uncontradicted testimony of Mr. Grace, establishes that it was intended and understood that petitioner should receive approximately \$100,000 for its good will and that petitioner would not have entered into the transaction on any other basis.

In rendering its decision herein the Tax Court completely disregarded all of the above evidence and

the applicable principles of law established by Court decisions and determined that no part of the consideration received by it was received for its good will or going concern value. Petitioner respectfully submits that the determination of the Tax Court is not supported by the evidence or the applicable principles of law and that said determination is clearly erroneous and should be reversed.

III. THE DE TURK WINERY BUSINESS WAS A DISTINCT BUSINESS UNIT OF PETITIONER AND GAIN DERIVED FROM THE SALE OF THAT UNITARY BUSINESS IS A CAPITAL GAIN.

The evidence establishes that the DeTurk Winery business consisting of the manufacture and sale of wines, was one of several different business operations in which the petitioner was engaged (R. 49, 50, 104.)

In the case of *Graham Mill and Elevator Co. v. Thomas*, 6 Cir., 1945, 152 F. (2d) 564, a corporation sold all of the assets making up four of its branch operations. The Court in sustaining the Commissioner and the District Court, held that a branch operation is a business entity and the sale resulted in a capital gain, though individual assets of the branch included inventory and other non-capital assets. *The Court observed that since the sale was not made in the course of business to customers but was a part of the ending of the business, the transaction constituted a sale of capital assets.*

The day after the above case was decided the U. S. Circuit Court of Appeals for the Second Circuit decided the case of *Williams v. McGowan*, 2 Cir. 152 F (2d) 570. In that case a surviving partner sold the business once conducted by the partnership. The District Court held that the sale was a sale of a business entity and any gain derived therefrom was capital gain. The Circuit Court, one Judge dissenting and agreeing with the District Court, held that the taxpayer had acquired the business and property of the partnership upon the death of his partner and had not sold the partnership interest as a distinct interest but had sold the individual assets, and gain or loss had to be computed as to each asset. The Court did recognize that *a partner's interest in a going firm* is for tax purposes to be regarded as a "capital asset" (citing *Stilgenbaur v. United States* 9 Cir., 115 F (2d) 283, 25 AFTR 966 and other cases.)

The distinction between the *Graham Mill* case, supra and the *William* case, supra, may be indicated by a remark made by the Tax Court in the case of *James H. Adamson* T. C. Memo Docket 3154, decided December 11, 1946 which case was cited with approval in the case of *United States v. Adamson*, 9 Cir., 1947, 161 F (2d) 942, as follows:

" . . . we think it cannot be said that this petitioner . . . sold his partnership interest as such, *at least not in the sense that one sells an interest in a 'going concern'.*" (Italics ours.)

It would appear from the reasoning in the *Graham Mill* case, supra, from the dissenting opinion in the

Williams case, *supra*, and from the *Adamson* case, *supra*, that if a taxpayer disposes of a going concern as such, it disposes of a capital asset entity for tax purposes, without regard to the asset components thereof, and any gain resulting from the transaction is taxable as a capital gain. *It is emphasized that this was the very principle which the Commissioner advanced in the Graham Mill case when it meant more tax to have the transaction treated as a capital asset transaction. Since the District Court and the Circuit Court of Appeals sustained the Commissioner, he should be forced to adhere to his position and should not be permitted to blow hot and cold depending upon how the tax is affected.*

It is respectfully submitted that since the petitioner disposed of the DeTurk Winery business as a "going concern," which it had conducted for many years, the entire profit from the transaction with Garrett & Co. should be taxed as a long-term capital gain.

The Tax Court dismissed this contention on the ground that under its construction of the transaction there was not a sale of the business as a unit but a mere sale of wine and barrels and a lease of the winery. For the reason set forth in the preceding section of this brief petitioner submits that the transaction between petitioner and Garrett & Co. was intended to be and actually was a sale of petitioner's entire winery business and was not a mere sale of wine and barrels. Petitioner further submits that the Tax Court erred in determining that the trans-

action was not a sale of the entire business as a unit the gain from which constituted long term capital gain under the authorities cited.

IV. PETITIONER'S INVENTORY OF WINE WAS CONVERTED INTO A CAPITAL ASSET WHEN PETITIONER DETERMINED TO DISPOSE OF ITS WINERY BUSINESS AND THE ASSETS THEREOF AND THE GAIN REALIZED UPON THE SALE CONSTITUTED LONG TERM CAPITAL GAIN.

The record establishes that in 1942 just prior to the crushing season—October and November—the petitioner decided to sell its winery business. The record indicates that though it manufactured but 4,959 gallons of wine in 1942, compared with a usual annual production of approximately 200,000 gallons of wine, it continued to conduct its business and sold wines up to January 1, 1943 (R. 104.) The record indicates that in January, sometime prior to January 20, 1943, the petitioner did transfer everything connected with its winery business to Garrett & Co. The question arises, did the item of wine inventory which had been an inventory asset held for sale to customers in the ordinary course of business lose that characteristic and become a capital assets prior to the sale to Garrett & Co.

It appears that whether or not a sale or exchange involves a capital asset depends upon the nature of the asset *at the time of the sale or exchange*. The Commissioner's regulations, Regulation 111, Sec. 29.117-1 concede this specifically as to certain types

of capital assets and since the statutory definition of capital asset is the same as to all types of capital assets it would appear that the said regulation would apply to all types of capital assets.

In the case of *Lurie v. Commissioner*, 9 Cir., 1946, 156 (2d) 436, the petitioner held unregistered notes for over 24 months. Just before the notes were retired they were put in registered form. As unregistered notes they were not capital assets, as registered notes they were. The taxpayer reported the gain on the retirement as long term capital gain. The Commissioner and the Tax Court treated the gain as ordinary income because the notes had not been held *as registered notes* for the 18 months holding period to qualify as long term capital assets. The Circuit Court reversed the Tax Court holding that so long as the asset was a capital asset at the time of the sale or exchange, and as long as it had been held the necessary period, regardless of whether during that entire period it was a capital asset, the gain from the sale or exchange was a long term capital gain under the statute.

The same principle was applied in the case of *Commissioner v. Euleon Jock Grocery*, 5 Cir., 1947, 159 F (2d) 324.

It would follow from these decisions, that if the wine inventory lost its characteristic as an inventory or stock in trade asset at any time prior to the sale to Garrett & Co., the gain on the sale of the wine, excepting on 4,959 gallons manufactured in October,

1942, would be taxable as long term capital gain because all the wine excepting the 4,959 gallons, was held over 6 months. The question arises as to whether the wine did change its characteristic prior to the sale to Garrett & Co.

The authorities are consistent in the proposition that where a taxpayer is no longer carrying on a business the assets which previously qualified as business assets or stock in trade, lose their characteristic as such and become capital assets.

In the *Adamson* case, T. C. Memo, supra, the Tax Court held that property which constituted stock in trade of a partnership was no longer stock in trade after the partnership had gone out of business and the property was being held for "division and distribution."

In *Three States Lumber Co.* 7 Cir., 1946, 158 F (2d) 61, the Court in reversing the Tax Court held that in a case where the taxpayer had quit the lumber business and was selling its timber in "activities incidental to an orderly liquidation" the timber was no longer property held primarily for sale to customers in the ordinary course of business but was a capital asset.

In the two cases above cited there was a substantial lapse of time between the going out of business and the disposition of the assets, but isn't this just a matter of degree? If it is the going-out of business, if it is the change in business, or if it is the change from holding of the asset for sale to customers in

the ordinary course of business to a holding of it for sale in some other manner or for some other purpose, then that change takes effect *at the time* the reason for the change takes place, and whether the asset is sold 10 days or 10 years after the change becomes effective, the treatment of the sale for tax purposes would be the same.

In this case the petitioner's business of manufacturing and selling wine consisted of making wine, aging it for the customary time of 6 months to 2 years and then selling it to its trade customers. In conducting this business it always had a stock of salable wine available while other wine was in the necessary aging process. The petitioner was not in the business of selling its entire stock of wine at one time, together with all equipment and cooperage. (*Butler Consol. Coal Co.* 6 TC 183.) From January 1, 1943 the time this taxpayer's negotiations with Garrett & Co. reached the stage where the sale to Garrett & Co. seemed assured and the petitioner discontinued its regular business sales, the wine inventory was no longer held for sale to customers in the ordinary course of business, but became one of the component parts of a group of assets which were held for and later transferred in an isolated transaction, which was a type of transaction of an entirely different nature than the transactions theretofore had in the ordinary course of the business of manufacturing and selling wine. The sale to Garrett & Co. was not a sale to a customer in the ordinary course of business, and therefore when the wine became an asset held for

that purpose, whether for one day or 20 days it was no longer an asset held for sale to customers in the ordinary course of business.

It is respectfully submitted that the characteristic of petitioner's stock of wine was changed to a capital asset when held for sale to Garrett & Co. in an isolated transaction and therefore excepting as to 4,959 gallons which had not been held for 6 months and the profit on the sale of which can be computed from the record the profit on the sale of the wine to Garrett & Co. should be treated as a long-term capital gain.

Petitioner respectfully submits that the Tax Court erred in determining that the wine was not converted into a capital asset prior to the sale to Garrett & Co. and in determining that the gain from the sale of the wine was ordinary income.

V. CONCLUSION.

Petitioner respectfully submits:

(1.) That the evidence and authorities cited and discussed in this brief clearly establish that in the transaction between petitioner and Garrett & Co., petitioner sold its entire winery business including its good will and that at least \$100,000 of the consideration received by petitioner was received by it for its good will.

(2.) That since the transaction was a sale of its entire winery business the entire gain consti-

tuted long term capital gain and not ordinary income.

(3.) That prior to the sale the wine inventory was converted into a capital asset and the gain realized from the sale of the wine (except 4,959 gallons) was long term capital gain and not ordinary income.

Petitioner further respectfully submits that the determination of the Tax Court that the transaction between petitioner and Garrett & Co. was merely a sale of wine and barrels and a lease of the winery and that the entire gain constituted ordinary income is clearly erroneous and should be reversed.

Dated, San Francisco, California,

October 15, 1948.

Respectfully submitted,

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Attorneys for Petitioner.



No. 11976

**In the United States Court of Appeals
for the Ninth Circuit**

GRACE BROS., INC., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

**ON PETITION FOR REVIEW OF THE DECISION OF THE TAX
COURT OF THE UNITED STATES**

BRIEF FOR THE RESPONDENT

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FILED

DEC 6 1948

PAUL P. O'BRIEN,

CLERK

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COURT OF THE UNITED STATES*

BRIEF FOR THE RESPONDENT

OPINION BELOW

The opinion of the Tax Court (R. 18-30) is reported in 10 T.C. 158.

JURISDICTION

This petition to review the determination of the Tax Court involves a deficiency in income and excess profits taxes for the year 1943. A deficiency of \$114,190.49 for excess profits tax and \$10,740.53 for declared-value excess profits tax, and an overassessment of \$10,731.62 for income tax was determined by the Commissioner of Internal Revenue, who on September 20, 1945, notified the taxpayer thereof, pursuant to Section 272 of the Internal Revenue Code. (R. 10-12.) The taxpayer, on December 10, 1945, pursuant to Section 272, Internal Revenue Code, filed a petition with the Tax Court of the

United States to review the Commissioner's determination (R. 1), and thereafter on February 24, 1947, filed an amended petition in which it alleged that it had overpaid its excess profits taxes for the year 1943 by the amount of \$23,913.11 (R. 4-9). On March 19, 1947, the Commissioner filed an answer to the amended petition denying the taxpayer's claims. (R. 16-18.) On January 27, 1948, the Tax Court promulgated its findings of fact and opinion (R. 18-30) and on April 5, 1948, entered its decision determining a deficiency in the taxpayer's excess profits taxes for the year 1943 in the amount of \$124,073.01 and an overpayment in declared-value excess profits tax in the amount of \$240.04 (R. 31).

The taxpayer on June 14, 1948, pursuant to Section 1141(a) of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948, filed a petition for review by this Court of the decision of the Tax Court. (R. 32-38.)

QUESTIONS PRESENTED

1. Whether the Tax Court erred in holding that no portion of the consideration received by the taxpayer for the sale of its wine inventory represented payment for the good will of the taxpayer's business.

2. Whether the Tax Court erred in holding that the transaction under consideration was not the disposition of a "unitary business" but rather the sale of particular assets which must be treated as ordinary income.

3. Whether the Tax Court erred in holding that the taxpayer's stock in trade was not converted into a capital asset by virtue of its decision to discontinue business.

STATUTES AND REGULATIONS INVOLVED

These are found in the Appendix, *infra*.

STATEMENT

The facts as found by the Tax Court (R. 20-24) may be summarized as follows:

The taxpayer, a California corporation with principal place of business at Santa Rosa, California, keeps its books on an accrual basis of accounting and filed its 1943 income tax returns, prepared on that basis, with the Collector of Internal Revenue for the first district of California. In 1943 and for many years prior thereto it has engaged in various enterprises, including farming, grape growing and the manufacture and sale of wines and beer. All of its stock was owned by its president and manager, Joseph T. Grace, of Santa Rosa, a man active in numerous civic, financial, industrial and agricultural enterprises, and for over twenty years a vice-president of the Bank of America. (R. 20.)

In 1921 the taxpayer purchased a wine-manufacturing plant, long known to the trade as DeTurk Winery. It operated the plant until 1943, producing from grapes grown by it or bought from others sweet and dry types of wine and some brandies which it sold to a regular clientele partly in bottles bearing the label "DeTurk Winery" and partly in barrels to wholesale customers who bottled and sold it under their own labels. "The DeTurk Winery, Established 1876" appeared above taxpayer's name on its invoices. The product was accepted by the trade as a wine of high quality; it was successfully marketed, and the net profit from its sale for the years 1936-1942 was as follows (R. 20-21):

1936.....	\$26,610.18	1939.....	\$16,100.84
1937.....	33,184.93	1940.....	10,459.86
1938.....	20,377.92	1941.....	7,995.20
		1942.....	18,959.53

In 1941 the taxpayer's sales were 157,518 gallons of dry wine in bulk and 8,888 gallons in bottles at an average

price of 22.6 cents a gallon, and 46,943 gallons of sweet wine in bulk and 12,443 gallons in bottles at an average price of 37.2 cents a gallon. In 1942 it sold 114,046 gallons of dry wine in bulk and 7,028 gallons in bottles at 22.2 cents a gallon, and 46,009 gallons of sweet wine in bulk and 10,268 gallons in bottles at 36.8 cents a gallon. During the years 1936-1942 its average investment in this section of its business was \$150,000, of which roughly \$60,000 was attributable to the plant and \$90,000 to inventory. As dry wine should be held two years or more and red wine one year for aging, a substantial inventory was kept in stock. (R. 21.)

Finding his numerous activities excessive, Grace decided late in 1942 to discontinue the wine business, and the taxpayer limited its production for that year to 4,959 gallons extracted only from the grape supply grown by it, whereas normally its annual production was about 200,000 gallons. Nonetheless it had an inventory of 522,761 gallons at the end of the year, produced in 1942 and prior years. (R. 21.)

In November 1942 Grace advised L. A. Weller, an old acquaintance and vice-president of Garrett & Company, Inc., of New York, that he intended to abandon the wine business. Weller manifested interest, asking the quantity of wine available for sale; saying that his firm's lease on a California plant was about to expire, and making inquiry about a lease of the DeTurk Winery and the possibility of installing in it certain machinery. (R. 21-22.) After Weller's return to New York, Garrett & Company requested Grace by telegram of December 28, 1942, to submit details if "interested in selling your inventory and leasing winery." Grace replied the following day "that we have several purchasers for our inventory and lease of winery and distillery"; offered specified quantities of several types of wine at 40, 55, 60 and 65 cents a gallon, respectively,

and a lease "of winery, distillery and bonded warehouse" for five years at an annual rental of \$12,000. In further negotiation by telegraph, Grace inquired what part of the inventory was of interest, adding (R. 22):

* * * anxious to close deal immediately to get part of sales in this year income tax returns * * *.

Agreement was reached by telephone and confirmed by a telegram of Garrett & Company to Grace on December 31, 1942. By the contract Garrett & Company agreed to purchase all of the taxpayer's wine at 50 cents a gallon; to pay 20 per cent of the purchase price immediately, and to lease the winery for five years at \$10,000 annual rent. On the same day the taxpayer delivered 104,000 gallons; received \$52,000 therefor from Garrett & Company, and reported the profit on its 1942 income tax return. (R. 22.)

There remained 418,761 gallons of wine, carried on the taxpayer's books at \$79,046.33, consisting of 248,635 gallons of dry wine and 170,126 gallons of sweet wine. During 1943 this entire stock was delivered and the taxpayer received \$124,317.50 for the dry wine and \$94,862.41 for the sweet wine. The price paid for the latter was by agreement somewhat in excess of 50 cents a gallon because 73,628 gallons contained a higher sugar content than required by California standards. Garrett & Company also agreed to purchase 600 wine barrels at \$4 each. On January 20, 1943, the parties signed a detailed memorandum of the agreement, setting forth its terms as above described, and on January 30 they signed the contemplated contract of lease. By its terms the taxpayer leased to Garrett & Company the premises of the winery "together with all winemaking machinery and equipment located therein" and the right to use the spur track of a railroad on the east side of the property.

The annual rental was fixed at \$10,000; the term of the lease at five years with right of renewal for an additional five years. The lessee agreed to keep the equipment in good working order and in a reasonable state of repair; it reserved the right to remove all machinery and equipment installed by it within sixty days of the lease's expiration. The lessor reserved a small office and the use of well water on the leased premises for its adjoining cold storage plant. It agreed to carry fire insurance except on equipment installed by the lessee, and in case of damage to make repairs with due diligence. If the winery should be totally destroyed, the lease was to terminate. (R. 23-24.)

In giving possession to Garrett & Company the taxpayer surrendered its permit to manufacture and sell so that the lessee could procure a permit to operate on the premises; turned over to the lessee all its wine stocks, cooperage and labels, its list of customers and its regular staff of eight or ten experienced employees. Thereafter neither the taxpayer nor Grace engaged in making or selling wines. Garrett & Company paid rent under the lease to the end of April, 1944, when the parties terminated it by mutual agreement. On April 15, 1944, the taxpayer sold the winery to Taylor & Company for \$150,000. Taylor & Company was not a subsidiary of, or owned by Garrett & Company. (R. 24.)

In computing the taxpayer's income tax, declared value excess profits tax and excess profits tax for 1943, the Commissioner determined (1) that the taxpayer realized ordinary income of \$140,133.58 from the sale of wine in 1943, and not a capital gain in that amount as reported by it; and (2) that the taxpayer in 1943 realized a capital gain of \$99,002.64 from the sale of the winery. (R. 24.) Only the first of these determinations was disputed in the Tax Court, the parties having agreed that the gain arising from the sale of the winery

was taxable in 1944. (R. 30.) The Tax Court upheld the Commissioner's determination as to the first issue (R. 30) and from that decision the taxpayer petitioned for review.

SUMMARY OF ARGUMENT

The taxpayer during the latter part of 1942 sold its wine inventory and leased its winery plant to a competing wine manufacturer. The agreement was embodied in a written memorandum and a lease. The Tax Court held, despite the taxpayer's contention to the contrary, that it was not intended that anything more be sold other than as embodied in these documents. Accordingly, the gain realized on the sale of the wine inventory was to be reported as ordinary income and not long term capital gain under Section 117, Internal Revenue Code. No support is found in the record for the taxpayer's argument that it was intended to convey its good will, valued at \$100,000, except the unsupported testimony of the taxpayer's sole stockholder. Moreover, the record is replete with evidence which contradicts that testimony and squarely supports the Tax Court's conclusion regarding the character of the transaction.

The taxpayer's alternative contention that the transaction involved the sale of its business as a unit rather than as a sale of separate assets was likewise found by the Tax Court to be lacking in factual support and analysis of the record discloses that this conclusion is clearly correct.

The Tax Court similarly rejected the taxpayer's argument that a decision to terminate its business had the effect of converting its stock in trade into a capital asset, the sale of which yielded capital gain. No such conversion could take place in view of the nature of the asset, i.e., stock in trade, and in any event, the asset was not held as a capital asset for more than six months so as to yield capital gain.

ARGUMENT

The Tax Court correctly held that the taxpayer sold its wine inventory and leased its winery and that the gain derived therefrom was ordinary income and not long term capital gain

During the latter part of 1942 the taxpayer, a corporation engaged in the manufacture and sale of wine, negotiated with a representative of Garrett & Company, a competing wine manufacturer, for the sale of its wine inventory and the lease of its winery plant. These negotiations were concluded on December 31, 1942, following a series of telegrams and telephone conversations. The results of the parties' agreement were embodied in a memorandum dated January 20, 1943, and a lease dated January 30, 1943.

The Tax Court held that the written agreement dated January 20, 1943, reflected the complete understanding of the parties and despite the taxpayer's contention to the contrary, nothing (such as good will) was sold or intended to be sold except as therein stated. The Tax Court likewise rejected as lacking factual support the taxpayer's alternative contention that the transaction involved the sale of its entire wine business as a unit (and not separate assets) and should therefore be treated as giving rise to capital gain. Lastly, the Tax Court rejected the argument that the taxpayer's decision to give up its business converted its stock in trade to a capital asset, the sale of which yielded capital gain. All three contentions are now advanced on this appeal.

A. The Tax Court correctly held that no part of the consideration received by the taxpayer was for the sale of its good will

The taxpayer's chief contention is that at least \$100,000 of the \$219,179.91 received by it from Garrett & Company in 1943 under its contract for the sale of

wine represented consideration for the sale of its good will. The Tax Court held (R. 27) that on the evidence it was “unable to make such a finding or to hold that the sale contract covered any more than its terms indicate”. We submit this conclusion to be clearly correct and—in the light of the record—phrased even more conservatively than necessary.

Whether the taxpayer contracted for the sale of its good will presents a pure question of fact. Under familiar rules respecting the scope of judicial review, the findings made by the Tax Court in this regard may not be set aside unless “clearly erroneous”. Section 1141(a), Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948, Public Law 773, 80th Cong., 2d Sess.; Rule 52(a), Federal Rules of Civil Procedure. It is the function of the Tax Court to weigh the evidence, to judge the credibility of the witnesses and to draw inferences from the facts. It was not obliged as the taxpayer urges (Br. 20-22) to reach its conclusion exclusively on the basis of the testimony of the taxpayer’s sole stockholder (Joseph T. Grace, hereafter referred to as Grace) merely because it may have been uncontradicted by other oral testimony. *Birnbaum v. Commissioner*, 117 F. 2d 395 (C.C.A. 7th); *Cohen v. Commissioner*, 148 F. 2d 336 (C.C.A. 2d); *Jergens v. Conner*, 125 F. 2d 686 (C.C.A. 6th); *Greenfeld v. Commissioner*, 165 F. 2d 318 (C.C.A. 4th); *O’Laughlin v. Helvering*, 81 F. 2d 269 (App. D. C.); *O’Dwyer v. Commissioner*, 110 F. 2d 925 (C.C.A. 5th).

Even conceding the existence of a rule which accords weight to the uncontradicted though unsupported testimony of an interested witness where the facts otherwise permit the conclusion for which his testimony is offered (*Foran v. Commissioner*, 165 F. 2d 705 (C.C.A. 5th)) that rule is strictly limited to cases in which the uncontradicted testimony of unimpeached witnesses is con-

sistent *with facts actually proved* and has no application to a case in which every other proven fact is inconsistent with the so-called uncontradicted testimony (*Quock Ting v. United States*, 140 U. S. 417, 420-421, 422). And in the context of this case we submit that the rule is completely inapplicable because every proven fact tends to discredit and make wholly improbable the testimony so strongly relied upon.¹ The Tax Court in its opinion recognized the numerous weaknesses of Grace's testimony, and analysis of the record discloses numerous inconsistencies so basic as to justify the conclusion that not only was the Tax Court's decision not "clearly erroneous" but that it was the only correct one.

The form in which the parties here chose to mold the transaction is plainly disclosed by the documents which they executed. They are the best evidence of what they intended to do and of what they accomplished. Apart from the testimony of Grace, the facts prove a sale barren of anything but the taxpayer's wine inventory (and about 600 wine barrels). Not a word even implying the sale of something in addition thereto can be found in the telegraphic communications which pre-

¹ Since the oral testimony of Grace (R. 52-92) tends largely to supply alleged omissions and to contradict the express terms of the written contract of sale and lease entered into by the taxpayer and Garrett & Company there would appear to have been a sufficient basis for the complete rejection of such testimony by the Tax Court under the familiar rule that all prior and contemporaneous oral understandings are merged in a written contract which purports to reflect the entire agreement of the parties. *Gaylord v. Commissioner*, 153 F. 2d 408, 415 (C.C.A. 9th); *Jurs v. Commissioner*, 147 F. 2d 805, 810 (C.C.A. 9th); *Sherman v. Commissioner*, 76 F. 2d 810 (C.C.A. 9th). However, having permitted the taxpayer's principal stockholder so to testify the Tax Court manifestly was under no obligation to give conclusive effect to such testimony and to disregard the express terms of the written contract embodying their agreement. *Woodall v. Commissioner*, 105 F. 2d 474 (C.C.A. 9th); *Boland v. Commissioner*, 118 F. 2d 622 (C.C.A. 9th); *Jurs v. Commissioner*, *supra*; *Gaylord v. Commissioner*, *supra*.

ceded the execution of the formal contract of sale; or in the memorandum contract itself; or in the lease of the winery; or in letters subsequent to the sale between the parties. Moreover, the contrary is strongly indicated not only in all of the documentary evidence but also in the inability of Grace to explain how the amount of good will allegedly included was computed on the separate items of the wine inventory; in the absence of evidence that the December 1942 market prices of the various wines sold by the taxpayer were lower than the prices quoted; in the attempt of Grace to exaggerate the importance of the so-called "organization of key men" transferred to the purchaser; in the cancellation by Garrett & Company of the lease after approximately one year of occupancy; in the failure of the taxpayer to show that the trade name allegedly contracted for was ever in fact used by the purchaser; and in the utter lack of documentary evidence to corroborate any of the claims of the taxpayer.

Each of the above-named items of evidence will be separately analyzed in the following discussion.

The telegraphic communications. Grace testified (R. 53, 55-56) that prior to the interchange of telegrams between him and Garrett & Company he met Mr. L. A. Weller, the executive vice president of the latter company, in Fresno and that at that time preliminary discussions were commenced by Weller's statement that he had heard that Grace had "some wine to sell" (R. 53). Grace said that he told Weller that he wanted to get out of the wine business and (R. 53-54)—

I wouldn't sell the wine inventory unless I sold everything in connection with the wine business, that is, winery and wine inventory and the good will in it—everything that had to do with it * * *.

In addition, Grace estimated that the winery was worth \$125,000 and the wine inventory and good will, \$250,000, a total of \$375,000. (R. 54.)

Grace, in addition, testified that Weller also said² (R. 56)—

I can give you what you ask for your wine and everything that goes with it, the good will, which would be equivalent to \$250,000. * * * If I give you 50 cents a gallon, that will give you what you are asking.

It is perhaps fair to state that these two portions of the testimony are the crux of the taxpayer's case that the parties contracted for the sale of good will.³ Yet the contradiction of this testimony by the proven facts is so marked as easily to justify any doubts the Tax Court might have had as to Grace's credibility or as to the taxpayer's failure to support its case by evidence. Thus, for example, despite Grace's alleged initial refusal to sell any wine inventory unless everything connected with the business, including the winery, was *sold* the fact is that the winery was merely *leased* to Garrett & Company. Grace's attempt to equate the leasing of the winery to a sale (R. 55), on the theory that the investment by Garrett in the winery would make it uneconomical for Garrett not to purchase, topples when the record discloses (R. 106-107) that in less than 15 months Garrett surrendered the lease and abandoned

² This alleged statement of Weller apparently is deemed crucial by the taxpayer since in its "Summary of pertinent facts" (Br. 17), it is presented and italicized as if it were a fact of record or at least as if it were Weller's *testimony* rather than, as is the case, the hearsay testimony—self-serving in the extreme—of Grace himself. (Weller, it should be noted, had died prior to the date on which this case was tried in the Tax Court. (R. 79.))

³ These statements also provide the chief basis for the alternative argument (Br. 39-42) that the transaction involved the sale of a "unitary business".

the winery, and it was then sold by the taxpayer to a third party.

Further, as was stressed by the Tax Court (R. 26-27), it taxes the credulity that parties who have discussed the sale of a wine inventory and intended thereby to sell a going business inclusive of good will valued at \$100,000, for a total price of \$250,000 (or in the alternative for a compromise price of 50 cents a gallon) should never thereafter in their telegraphic communications or in their formal contract of sale have referred to such good will, to the price of \$100,000, or to anything other than the wine itself. Rather, the taxpayer's first formal telegraphed offer to sell (R. 71-72) carefully listed its entire wine inventory according to type and price (40 cents and 65 cents per gallon). The subject matter of the telegram was otherwise limited to the statement that the taxpayer had (R. 71) "several purchasers for our inventory and lease of winery and distillery. Also bonded warehouse". There was not a word about the sale of the so-called "business" of the taxpayer. A second telegram sent that same day added other types of wine to the inventory listed in the first telegram (at 60 cents per gallon).

Garrett & Company responded with a suggestion that it merely take a *portion* of the wine inventory—a suggestion, of course, wholly inconsistent with the purchase of the taxpayer's "business". Significantly, the taxpayer responded by asking (R. 73) "What part of inventory are you interested in. Stop. What are your ideas on rental of plant". The next telegram dated December 31, 1942, seems to provide a conclusive showing of the parties' intention, for, in it, Garrett & Company confirmed the telephonic agreement into which the parties had entered (R. 73-74) "relative to lease of winery and purchase of bulk wines".

We submit that this interchange of telegrams wholly

belies Grace's testimony, and unquestionably justified the Tax Court in concluding (R. 25) that it could not find "an offer upon the evidence adduced" to sell not merely the wine but also the good will of the business.

The memorandum dated January 20, 1943. Following the extensive negotiations during the last few days of December 1942 resulting in the telegraphic contract, a lengthy memorandum dated January 20, 1943 (R. 111-116), was prepared by Grace or his attorney in accordance with Grace's ideas and decisions (R. 81). This was signed by Weller and Grace. The memorandum, in summary, restated the understanding of the parties, as evidenced by the telegrams, that the taxpayer "has sold and said Garrett & Company, Inc., has bought as of December 31, 1942, 104,000 gallons of wine situate at DeTurk Winery, at Santa Rosa, California, for the sum of \$52,000.00 * * *" and the taxpayer (R. 111)—

agrees to sell and said Garrett & Company, Inc., agreeA [sic] to buy, all of the remainder of that certain inventory of wines now on hand at said DeTurk Winery consisting of approximately 416,000 gallons, including both sweet and dry wines, at the purchase price of fifty cents (50¢) per gallon.

Further provision was made for the payment of the balance of the wine as shipped. It was also stated that it was understood "that the inventory of wine sold approximates 520,000 gallons" (R. 112), and that 80,000 gallons of wine were to bear an increased price over and above the purchase price of fifty cents per gallon. In addition, provisions were made with respect to other portions of the inventory not up to California standards of quality (R. 112-113), for the payment of taxes assessed against a certain portion of the wine inventory and for the payment of fire insurance premiums on the wines by the buyer (R. 113). Additional provision was

made for the sale of approximately 600 wine barrels on hand at the winery at the price of \$4 each. There then followed elaborate provisions with respect to the lease of the DeTurk Winery and the adjoining property.

It seems not unfair to suggest that if this agreement—so painstakingly prepared and presumably with legal assistance—was intended to embrace a transaction whereby an entire business was to be transferred to the purchaser it fell far short of its purpose. The agreement discloses a most meticulous concern with the wine inventory and with nothing more.

Presumably if there were to be a transfer to the purchaser of the seller's stock of bottles (R. 58), its list of customers (R. 61), its highly trained "organization". (R. 61) and its "cooperage" (R. 24), some mention of these items would have been made. Presumably, too, there would have been some reference to the obligations incurred by the taxpayer and its stockholders in connection with such a sale. One might reasonably have expected to find a provision under which the taxpayer and its stockholders agreed not to compete with the purchaser in the wine business, or to use the trade name and label, or the list of customers assigned, or to "pirate" the "key men" of the organization. Nor would it be unusual to find some reference to the disposition of the taxpayer's accounts receivable and payable. But on a record barren of a single reference to ought save the wine inventory, the conclusion is a necessary one that the mere testimony of Grace must fall under the weight of the documentary evidence presented.

The lease dated January 30, 1943 (R. 116-120). Here again, we have documentary evidence supporting the Tax Court's conclusion. The lease gave possession to Garrett of the premises on which the DeTurk Winery was located as well as (R. 117) "all-wine making ma-

chinery and equipment located therein and the right and privilege to use the spur track" of a railroad running alongside of the plant. A transfer of an "entire business" to a purchaser would appear to be incompatible with the mere lease of all the wine making machinery. This inconsistency takes on added significance when viewed against the fact, suggested by the record, that the location and size of the manufacturing plant are of some importance in the wine making industry. (R. 55-56.)

The L. A. Weller Letters (131-138). The taxpayer, as shown, was unable to offer a scintilla of written evidence to buttress its case. Moreover, in each of the letters written by L. A. Weller regarding the transaction there is a corresponding failure to mention anything other than the sale of the wine inventory. Further, in the letter dated November 5, 1946 (R. 135-138), there is a clear-cut contradiction of Grace's testimony regarding one aspect of the transaction which bears materially upon the whole. Grace, it will be remembered, testified (R. 53-54) that in the personal conversations between the two prior to the interchange of telegrams he had informed Weller that the wine inventory would not be sold unless everything in connection with the business, including the winery and the good will, were also sold; and that the winery was worth \$125,000, the wine inventory and good will, \$250,000, a total of \$375,000 for everything. Weller's letter stated (R. 135) "I find nothing in the exchange of our telegrams about his wanting to sell us the plant or do I have any recollection of it * * *." Certainly the failure to recall the reference to the sale of the winery at the price of \$125,000 in the very same conversation in which the sale of the good will was allegedly discussed casts a strong shadow of doubt upon Grace's testimony regarding that conversation. Beyond ques-

tion, it presents a material contradiction upon which a trial court may base its conclusion to disregard other portions of the challenged testimony.

Further analysis of the Weller letter shows no mention of any sale of the "business" or good will. On the contrary, the sale is specifically referred to as a "deal * * * for the Santa Rosa wine and plant lease." (R. 135.) Thus, the only other person whose description of the sale could conceivably have accorded with that of the taxpayer's failed in any respect so to do.

The inclusion of good will in the telegraphed offer. Grace apparently recognized the rather strong conflict between his testimony that a total price of \$250,000 had been fixed by him for the entire wine inventory, inclusive of good will, and the fact that in the offer made subsequently thereto to Garrett by telegram dated December 28, 1942 (R. 71-72) the separate types and grades of wine were listed with prices of 40 cents, 65 cents and 60 cents. At these prices the inventory would have sold for \$280,000. In addition, Grace had testified that the parties had generally agreed on a price of 50 cents per gallon although the prices as offered averaged about 57 cents per gallon.⁴ Grace attempted to explain away these inconsistencies on the ground that the prices were roughly computed to include the good will sought to be sold. (R. 83.) Yet on cross-examination (R. 88-89) he admitted that the listing of prices was not done on the basis of including good will with reference to each type of wine. Again, a self-contradiction greatly weakening the probative force of his testimony.

⁴ The trial court's recognition of this conflict in Grace's own testimony is indicated by its cogent questions (R. 83) with reference to the fluctuation of prices on different types of wine as compared with a flat price on all wines and the difference between the figure of 50 cents per gallon and the average of the prices listed in the offer of December 28.

Market prices of wines in December 1942. The taxpayer's effort to contradict the express terms of the agreement depends, as just shown, in large measure upon a showing that the price or prices quoted for the wine inventory included a substantial provision for good will. Corroborative evidence thereof might possibly have been found in the fact—if it was a fact—that the market prices for the taxpayer's grades of wine in December 1942 were substantially lower than the prices quoted to Garrett. For this reason it seems clear that the Tax Court was quite justified in concluding (R. 27) that it was significant that the taxpayer—

offered no evidence of the market price of its grades of wine in December 1942 apart from Grace's general testimony that the price paid by Garrett & Co. was excessive by \$100,000.

The taxpayer, however, urges (Br. 36-37) that this omission is supplied by that portion of the stipulation of facts (R. 103-108) which showed the average prices at which the taxpayer had been selling its wine in the year 1942; that applying such average price to the number of gallons sold there would have been received about \$100,000 less than the amount actually received. This the taxpayer now offers in lieu of the vitally essential evidence not elsewhere to be found in the record. The short answer to this is that an average price at which wine is sold during the year gives no possible basis on which to determine what the price of such wine is at any one point of the year. Obviously, the price in December may so far exceed the price during the early part of the year⁵ as to completely destroy the probative value of such evidence to support

⁵ Some indication that such, in fact, was the situation in 1942 may be found in Grace's testimony that conditions [in June 1942] "were getting better". (R. 60.)

the conclusion desired by the taxpayer. Yet the taxpayer further argues (Br. 36-37) that the Commissioner "was necessarily fully informed of the price at which wine was sold in December, 1942" and that "there can be no doubt that" he "would have introduced such fact in evidence". But we think it almost too plain to require statement that the burden of presenting evidence in this case lay with the taxpayer and not with the Commissioner. That burden—which it so obviously failed to carry—may not now be supplied by mere argument.

The organization of "key men". In addition to the direct contradiction within Grace's testimony there is also to be found a rather flagrant exaggeration obviously offered for self-serving motives. For instance, Grace sought to create the impression that the employees of Grace & Company were an organization of "key men" with valuable and extensive training in the "art of wine making" (R. 57) which enhanced the value of the business (R. 52-53, 90) and if transferred to the purchaser was to be included in any consideration of the value of the taxpayer's good will.⁶ On cross-examination he disclosed for the first time that this valuable organization consisted of "three or four key men". (R. 77.) The "organization" included "about eight, maybe ten" men to do the ordinary work. (R. 77.) It is rather informative in this connection to refer to Exhibit 4-D. (R. 121.) There a breakdown of the taxpayer's winery operations for 1942 discloses that the only labor or salary costs incurred were \$6,134.32 for all operating labor, \$1,173.70 for all bottling labor and \$3,398.80 for all salaries and

⁶ Since the decision to remain with Garrett & Company rested with the employees themselves (*cf.* Grace's testimony, R. 57) it would appear questionable whether the taxpayer had the power or right to "transfer" to Garrett its "organization" by any means which would entitle it to include that organization in its good will evaluation.

commissions paid as selling expenses. Thus this "valuable organization" of key men (some 3 or 4, or 8 or 10) must necessarily have received but a small portion of the entire \$10,700 paid throughout 1942 for all types of labor, salary and commissions. Testimony of this character, indicating a deliberate effort to color the facts, suggests the substantial infirmity of the taxpayer's evidence.

The DeTurk trade name. As a measure of the value of the taxpayer's good will, testimony was offered to the effect that the wines produced by the DeTurk Winery were above average (R. 43) and that the DeTurk Winery, which sold its product under the DeTurk Winery label, had a good reputation in the wine industry which could properly be valued at five times its annual income (R. 44). No mention of the use of such label or trade name was, however, made in the telegrams or the memorandum agreement previously referred to. No restriction on the continued use of the name by Grace was embodied therein. Since the taxpayer continued to grow grapes (R. 64) the *opportunity* for its return to the wine-making business was ever present. Moreover, Grace was unable to state whether or not Garrett & Company in fact ever used the DeTurk wine label (R. 92). Finally, within 15 months the right to the use of that label or trade name was again apparently abandoned by Garrett when it yielded up its rights to the winery to Grace. All of this evidences a startling lack of interest by both parties in this trade name which had a value according to the taxpayer of a substantial portion of the \$100,000 allegedly paid in excess of the value of the inventory.

The absence of documentary evidence. From the foregoing it appears that the taxpayer's entire case must be sustained upon the testimony of Grace alone

for nowhere is there the slightest written evidence to aid the taxpayer. Yet not only were Grace and Weller involved in this transaction but there was testimony (R. 52-53) regarding conversations with other persons about the sale of the taxpayer's business as a unit and (R. 69-70) concerning discussions between Grace and his wife, both members of the board of directors, about the decision to dispose of the winery. But the testimony of none of the persons with whom such conversations were allegedly held was offered by the taxpayer. And, more significantly, it would seem that where at least four or five individuals deal in a transaction involving a quarter of a million dollars some writing would be made at some point in the negotiations in which mention would be made of so vital a factor as the disposition of good will, the right to engage in the business and the use of the trade name. But, as previously stated, not a word appears any place concerning restrictions upon the taxpayer's continued dealings in the wine business in competition with Garrett, its use of the DeTurk Winery label or continued solicitation of the list of customers transferred to Garrett.⁷

For all of these reasons therefore we submit that the factual case attempted to be made by the taxpayer falls before the weight of the record.

Before the Tax Court, as here (Br. 22-35), the taxpayer sought the aid of a legal presumption to demonstrate that it had sold its good will. The presumption relied on is to the effect that a profitable business is deemed to have a good will value and when

⁷ Assuming, *arguendo*, that all the valuable tangibles and intangibles which go to make up the good will of a going business were contracted for by the parties, there would remain a serious doubt as to the value to the purchaser of such good will transferred without the slightest restraint on its immediate impairment by a seller who might reengage in the same business the very next day.

sold in its entirety a part of the consideration paid is attributable to such good will whether or not the contract of sale so specifies. *White & Wells Co. v. Commissioner*, 19 B.T.A. 416, affirmed, 50 F. 2d 120 (C.C.A. 2d); *Pfleggar Hardware Specialty Co. v. Blair*, 30 F. 2d 614 (C.C.A. 2d).

The Tax Court properly held (R. 26-27) that the presumption referred to could not apply to the facts of this case since the taxpayer had failed to prove that the entire business including good will of a value of \$100,000 had, in fact, been sold.

It is self-evident that if the transfer of an entire business carries with it a factor of good will, one must show that an entire business has been transferred in order to sustain the contention that the good will has been conveyed. And we think it would unduly burden this discussion to refer again to the numerous factual portions of the record which demonstrate beyond debate that the transaction merely involved the sale of the taxpayer's wine inventories and the lease of its plant and equipment.

Moreover, the record further shows (R. 61-62) that in April 1944 when the taxpayer sold the winery and its equipment to Taylor and Company for a price of \$150,000, its cost basis was about \$51,000 so that it realized a gain of \$99,000. If we compare the gain so realized with Grace's estimate of \$100,000 for the entire good will of the business—or as he said (R. 62) “for the whole thing”—it becomes apparent that if any consideration was received by the taxpayer for its good will it was received in 1944, on the sale of its plant and equipment to Taylor and Company.

B. The Tax Court correctly held that the sale of the taxpayer's wine inventory and the lease of its winery was not the disposition of a "unitary business"

The taxpayer urges (Br. 39-42) that since the De-Turk Winery business was one of several different business operations in which it was engaged its disposition as a going concern was the sale of an entire business which should be taxed as a sale of a capital asset. The taxpayer recognizes (Br. 41) that its argument on this phase of the case rests on the same fact basis as the first contention. And the Tax Court dismissed this alternative argument since it could not accept the "factual premise" (R. 27) upon which it was based. The transaction, it held (R. 28), "was not single, but comprised a sale of wine and barrels and the lease of a winery". Reference was made to the fact that if the entire transaction had been a unit the profit therefrom would have been includible in the taxpayer's 1942 return and not its 1943 return since the contract of sale was entered into in 1942. Moreover, the profit so reportable would include the undisclosed profit from that portion of the wine delivered in 1942 and from the sale of barrels and from rent under the five-year lease as well as the gain on the wines delivered in 1943. Furthermore, the fact that the taxpayer reported the gain on the 104,000 gallons of wine billed to Garrett as ordinary income in 1942⁸ is evidence which indicates a contrary understanding of the nature of the transaction than

⁸ In order to get "part of sales" (R. 73) in its 1942 return "for income tax purposes" (as Grace explicitly stated in his telegram of January 1, 1943—R. 74-75) a portion of the inventory (104,000 gallons having a value of \$52,000) was billed to Garrett on December 31, 1942, immediately upon consummation of the agreement to sell.

that alleged. Although it is true that the position taken in a tax return does not ordinarily preclude a reversal by the taxpayer, the situation is otherwise,⁹ as here, the manner in which the transaction was reported offers strong evidence of the understanding and intention of the party to, and the nature of, the transaction.

In making this argument, the taxpayer relies upon *Graham Mill & Elevator Co. v. Thomas*, 152 F. 2d 564 (C.C.A. 5th), to support its view that a sale of all of the assets of a business is not made in the course of business and therefore constitutes a sale of capital asset. Not only does this case fail to aid the taxpayer's position, but it greatly weakens it. There the court was concerned with the sale of notes and accounts receivable and held that the selling of such assets prevented the resulting loss realized from being treated as an ordinary business loss.⁹ The evidence, the court said (p. 565), showed that the taxpayer—

was not in the business of selling notes and accounts, and had never so dealt with its notes and accounts before. * * * They represented the taxpayer's business capital, but were not a part of his stock in trade.

Thus, as the Tax Court pointed out (R. 29-30), the rationale of the decision indicates that if (as in the present case) the taxpayer's normal stock in trade had been the subject of consideration the decision would have been the reverse of what it was—since stock in trade is expressly excluded from the definition of Section 117(a), Internal Revenue Code, Appendix, *infra*.

⁹ Since in the *Graham Mill* case the "goods on hand"—i.e. the stock in trade was taken by the purchaser in each instance at inventory price (p. 565) no gain or loss was realized on the inventory and the issue present in this and *Williams v. McGowan*, 152 F. 2d 570 (C.C.A. 2d), could not arise.

Moreover, the case of *Williams v. McGowan*, 152 F. 2d 570 (C.C.A. 2d), directly repudiates the taxpayer's contention. There the taxpayer sold his business "as a whole" for a price of about \$64,000. The "business" sold included cash of \$8,100, accounts receivable of \$7,000, fixtures of \$8,000, a merchandise inventory of about \$49,000, and \$1,000 of accounts payable. Having suffered a net loss upon the transaction, the taxpayer attempted to report it as ordinary loss rather than a capital loss. The question raised was (p. 572) "whether upon the sale of a going business it is to be comminuted into its fragments, and these are to be separately matched against the definition in § 117(a)(1), or whether the whole business is to be treated as if it were a single piece of property". The court held in a concise but learned analysis that the definition of capital assets under Section 117(a)(1) of the Internal Revenue Code rejects the fiction of firm assets as an indivisible interest and accordingly that as to each of the items transferred (cash, receivables, fixtures and merchandise inventory) there must be separate consideration to determine whether it falls within the definition of Section 117. The conclusion naturally followed that the fixtures and the inventory were not capital assets since the former was subject to depreciation and the latter was "stock in trade" expressly excluded from Section 117.

Thus, assuming the factual validity of the taxpayer's argument that what was sold was a "unitary business", the *Williams* case demonstrates the irrelevancy of that fact to the question of whether the assets which go to make up the business may be treated as giving rise to capital gain rather than ordinary income.

The taxpayer's reference (Br. 40) to *United States v. Adamson*, 161 F. 2d 942 (C.C.A. 9th), obviously is

wide of the mark for that case held only that the disposition of certain rights in two contracts and against a judgment debtor constituted the sale of capital assets. It had no possible bearing on the sale of stock in trade in a going business.

Thus, since there is no factual basis for the view that a single capital item was sold and, for the further reason that the legal rule established by *Williams v. McGowan* precludes such a result, the Tax Court's conclusion that the profit from the sale under consideration was ordinary income is clearly correct.

C. The Tax Court correctly held that the taxpayer's wine inventory did not lose its character as stock in trade or as property held primarily for sale to customers in the ordinary course of trade or business by virtue of the taxpayer's decision to discontinue its wine business

The taxpayer's final contention (Br. 42-46) is that its wine inventory was converted into a capital asset when the decision was made to dispose of its winery business, and that the gain realized upon the sale of such a capital asset constitutes long term capital gain. The Tax Court held (R. 28-30) that a decision to liquidate one's business does not change the character of its stock in trade. The essential factor is, of course, the character of the property sold. Stock in trade may under the proper circumstances be converted into a capital asset. But the change will take place not merely by the decision of the taxpayer to sell *all* his inventory (a result generally hoped for by all inventory sellers) but by the modification of the use or purpose to which the property is placed. Thus, one who sells carpentry tools may convert them into capital assets by using them *as tools* rather than as stock in trade to be sold to customers.

In any event on this issue the holding of *Williams v. McGowan*, *supra*, is again decisive. There, as here, a decision to dispose of a going business was without effect on the character of the gain or loss on the separate assets to be sold.

In essence, this has been the view taken by this Court. Thus, in *Commissioner v. Boeing*, 106 F. 2d 305 (C.C.A. 9th), certiorari denied, 308 U. S. 619, it was held immaterial that a taxpayer engaged in the sale of cut logs from lands owned by him was motivated by *a desire to liquidate his investment*. The gain resulting from such sales—being from his “trade or business”—was ruled ordinary income. In the instant case, the wine sold was admittedly the stock in trade of the taxpayer. Since that factor was the basic question at issue in the *Boeing* case, it would appear that the same result should follow *a fortiori* in the present case. See also *Richards v. Commissioner*, 81 F. 2d 369, 373 (C.C.A. 9th), in which the motive to liquidate was likewise deemed without consequence on the sale of assets sold in the course of business.

The cases on which the taxpayer relies (*Three States Lumber Co. v. Commissioner*, 158 F. 2d 61 (C.C.A. 7th); *Adamson v. Commissioner*, decided December 11, 1946 (1946 P-H T. C. Memorandum Decisions, ¶ 46,286)) fail, on analysis, to lend any weight to this argument. The *Three States* case involved the sale of timber land whose value as a lumber producing asset had been exhausted. The sale was held (p. 64) to be an “orderly liquidation” of “capital assets [which had *always* been capital assets in the hands of the taxpayer] which no longer furnished income”. The case is clearly no authority for the view that stock in trade is converted into a capital asset merely because of the taxpayer’s decision to liquidate his

entire inventory. The *Adamson* case, already discussed *supra*, held only that the assignment of certain judgment rights against a debtor for, and certain reversionary rights in, a patent and trademark constituted a sale of capital assets since the taxpayer was not in the business of selling patents and trademarks. There was no issue as to the conversion of a non-capital asset to a capital asset.

By way of anticipating a further objection to its final contention, the taxpayer has also cited *Lurie v. Commissioner*, 156 F. 2d 436 (C.C.A. 9th), and *Commissioner v. Gracey*, 159 F. 2d 324 (C.C.A. 5th). These cases are submitted to fill the factual gap—not met by the argument that a conversion was effected—that in any event the so-called “capital assets” were not held for the statutory period of six months necessary to give rise to *long term* capital gain. (Section 117(a)(4), Internal Revenue Code, Appendix, *infra*.) Neither case is in point.

Lurie v. Commissioner, *supra*, involved the question whether amounts paid on the retirement of coupon notes should be considered as amounts received “in exchange therefor”, under Section 117(f), Internal Revenue Code, since only by virtue of that special provision is the retirement of a security regarded as the “exchange” of a capital asset. It needs no more to show that the case is irrelevant on the question whether stock in trade is subject to being “converted” must be held for more than six months thereafter in order to obtain the benefit of capital gains treatment.

The *Gracey* case, *supra*, likewise involved a section, Section 117(h)(1), Internal Revenue Code, which has no application to stock in trade, but which merely governs *exchanges* of one asset for another, in which event the holding period for the property transferred may be added to the period during which the property

received is thereafter held. But again, the reason lies in the express exception of Section 117(h)(1) to the general rule—an exception not accorded a taxpayer's inventory or stock in trade.

It is submitted, therefore, that stock in trade cannot be converted to a capital asset merely by a desire to liquidate; in any event, that such a "converted asset" must be held for more than six months to give rise to capital gain.

CONCLUSION

The decision of the Tax Court is correct and should be affirmed.

Respectfully submitted,

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DECEMBER, 1948.

APPENDIX

Internal Revenue Code:

SEC. 22 [as amended by the Public Salary Tax Act of 1939, c. 59, 53 Stat. 574, Sec. 1]. GROSS INCOME.

(a) *General Definition*.—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

* * *

(26 U.S.C. 1946 ed., Sec. 22.)

SEC. 117 [as amended by the Revenue Act of 1941, c. 412, 55 Stat. 687, Sec. 115, and the Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 150 and Sec. 151]. CAPITAL GAINS AND LOSSES.

(a) *Definitions*.—As used in this chapter—

(1) *Capital Assets*.—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23(1), or an obligation of the

United States or any of its possessions, or of a State or Territory, or any political subdivision thereof, or of the District of Columbia, issued on or after March 1, 1941, on a discount basis and payable without interest at a fixed maturity date not exceeding one year from the date of issue, or real property used in the trade or business of the taxpayer;

(2) *Short-Term Capital Gain*.—The term “short-term capital gain” means gain from the sale or exchange of a capital asset held for not more than 6 months, if and to the extent such gain is taken into account in computing net income;

* * * * *

(4) *Long-Term Capital Gain*.—The term “long-term capital gain” means gain from the sale or exchange of a capital asset held for more than 6 months, if and to the extent such gain is taken into account in computing net income;

* * * * *

(6) *Net Short-Term Capital Gain*.—The term “net short-term capital gain” means the excess of short-term capital gains for the taxable year over the short-term capital losses for such year;

* * * * *

(10) *Net Capital Gain*.—

(A) *Corporations*.—In the case of a corporation, the term “net capital gain” means the excess of the gains from sales or exchanges of capital assets over the losses from such sales or exchanges;

* * * * *

(26 U.S.C. 1946 ed., Sec. 117.)

Treasury Regulations 111, promulgated under the Internal Revenue Code:

SEC. 29.22(a)-10. *Sale of Good Will*.—Gain or loss from a sale of good will results only when the business,

or a part of it, to which the good will attaches is sold, in which case the gain or loss will be determined by comparing the sale price with the cost or other basis of the assets, including good will. (See sections 29.111-1, 29.113(a)(14)-1, and 29.113(b)(1)-1 to 29.113(b)(3)-2, inclusive.) If specific payment was not made for good will, there can be no deductible loss with respect thereto, but gain may be realized from the sale of good will built up through expenditures which have been currently deducted. It is immaterial that good will may never have been carried on the books as an asset, but the burden of proof is on the taxpayer to establish the cost or other basis of the good will sold.

* * * * *

SEC. 29.117-1 *Meaning of Terms.*—The term “capital assets” includes all classes of property not specifically excluded by section 117(a)(1). In determining whether property is a “capital asset,” the period for which held is immaterial.

The exclusion from the term “capital assets” of property used in the trade or business of a taxpayer of a character which is subject to the allowance for depreciation provided in section 23(1) and of real property used in the trade or business of a taxpayer is limited to such property used by the taxpayer in the trade or business at the time of the sale, exchange, or involuntary conversion. Gains and losses from the sale or exchange of such property are not subject to the percentage provisions of section 117(b) and losses from such transactions are not subject to the limitations on losses provided in section 117(d), except that under section 117(j) the gains and losses from the sale or exchange of such property held for more than six months may be treated as gains and losses from the sale or exchange of capital assets, and may thus be subject to such limitations. See section 29.117-7. Property held for the production of income, but not used in a trade or business of the taxpayer, is not excluded from the term “capital assets” even though depreciation may have been allowed with respect to such property under section 23(1) prior to its amendment by the Revenue Act of 1942. However, gain or loss upon the sale or exchange of land

held by a taxpayer primarily for sale to customers in the ordinary course of his business, as in the case of a dealer in real estate, is not subject to the limitations of section 117(b), (c), and (d). The term "ordinary net income" as used in these regulations for the purposes of section 117 means net income exclusive of gains and losses from the sale or exchange of capital assets.

* * * * *

Example (2). * * *

Section 117(a) (2) to (9), inclusive, defines "short-term capital gain," "short-term capital loss," "long-term capital gain," "long-term capital loss," "net short-term capital gain," "net short-term capital loss," "net long-term capital gain," and "net long-term capital loss." These terms are used in the subsequent subsections of section 117.

The phrase "short-term" applies to the category of gains and losses arising from the sale or exchange of capital assets held for six months or less; the phrase "long-term" to the category of gains and losses arising from the sale or exchange of capital assets held for more than six months. The fact that some part of a loss from the sale or exchange of a capital asset may be finally disallowed because of the operation of section 117(d) does not mean that such loss is not "taken into account in computing net income" within the meaning of that phrase as used in section 117(a) (3) and (5).

In the definition of "net short-term capital gain," as provided in section 117(a)(6), the amounts brought forward to the taxable year under section 117(e) are short-term capital losses for such taxable year.

Gains and losses from the sale or exchange of capital assets held for not more than six months (described as short-term capital gains and short-term capital losses) shall be segregated from gains and losses arising from the sale or exchange of such assets held for more than six months (described as long-term capital gains and long-term capital losses). The percentage brackets of section 117(b) have no application to corporations, corporate gains and losses being taken into account to the full extent, without regard to the length of time the

capital assets are held (though because of the limitation in section 117(d) such losses may not be deductible in full).

Section 117(a)(10) defines "net capital gain." In the case of a corporation the term "net capital gain" means the excess of the gains from sales or exchanges of capital assets over the losses from such sales or exchanges, which losses include any amounts brought forward pursuant to section 117(e).

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No. 11,976

IN THE

United States Court of Appeals
For the Ninth Circuit

GRACE BROS., INC.,

Petitioner,

VS.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONER'S REPLY BRIEF.

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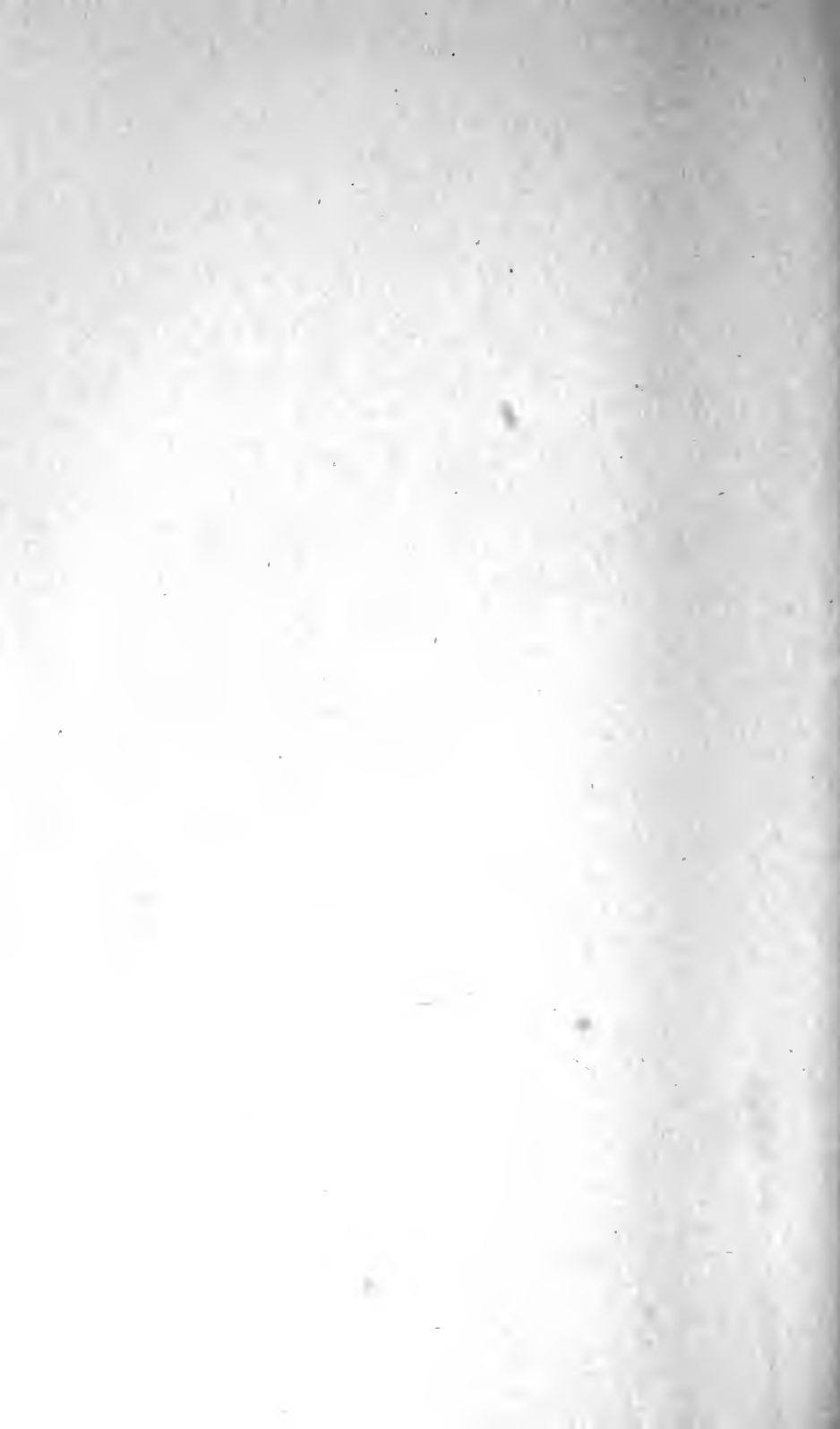
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PAUL P. O'BRIEN,

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PETITIONER'S REPLY BRIEF.

I.

AT LEAST \$100,000 OF THE CONSIDERATION RECEIVED BY PETITIONER FOR THE ASSETS OF ITS WINERY BUSINESS WAS RECEIVED FOR THE GOOD WILL OF THE BUSINESS AND CONSTITUTED CAPITAL GAIN.

A. Introductory statement.

Respondent's argument with regard to petitioner's contention that the transaction between petitioner and Garrett & Company, involved a transfer of the good will of petitioner's winery business is devoted primarily to a detailed discussion of the stipulated facts and evidence and his basic contentions appear to be (1) that in form the transaction was a sale of the wine inventory and a lease of the winery and equipment which did not involve petitioner's good will, and (2)

that the testimony of Mr. Grace is inconsistent with the form of the transaction and should be disregarded. Respondent completely disregards the substance and effect of the transaction and dismisses with brief comment the decisions which support petitioner's contention. Since petitioner has never denied that the transaction was in the form of a sale of wine, no attempt will be made in this brief to discuss the details stressed by respondent with regard to that point, and the argument will be confined to the basic issues and contentions.

B. The form of the transaction is not conclusive and should not prevail over the substance and effect.

In support of his contention that no part of the consideration received by petitioner was received by it for its good will, respondent emphasizes and relies primarily upon the fact that in the negotiations between the parties the written communications and agreements referred primarily to the wine inventory and made no mention of petitioner's good will. Petitioner has conceded from the outset that, in form, the transaction between it and Garrett & Company, was a sale of the wine inventory and a lease of the winery and equipment. Likewise petitioner has never contended that Garrett & Company sought to purchase or acquire the good will of petitioner's winery business. Petitioner's contention has been and now is that despite the form of the transaction, it did involve, in substance and effect, a transfer of petitioner's entire winery business including petitioner's good will. Petitioner has not challenged the facts as found by the

Tax Court but has based its appeal on the ground that the Tax Court erroneously interpreted the true nature of the transaction and based its decision entirely upon the form as set forth in the various written documents. Further discussion of the form of the transaction would be of no assistance in the determination of the real issue presented.

One of the basic principles of tax law is that taxation is a practical matter and that the determination of tax controversies should be based upon the substance and effect rather than the form of the transaction. This principle was established by early decisions of the Supreme Court of the United States and has been repeatedly announced by almost every Court. *Weiss v. Stearn* (1924), 265 U. S. 242, 68 L. Ed. 1001, 44 S. Ct. 490; *Helvering v. Tex-Penn. Oil Co.* (1937), 300 U. S. 481, 81 L. Ed. 755, 57 S. Ct. 569; *Watson v. Commissioner*, 9 Cir. (1932) 62 F.(2d) 35.

The decisions upon which petitioner relies and which petitioner contends decide the real issue involved in this case, establish that a transaction may involve a sale of the good will of a business even though the good will was not mentioned or specifically considered in the negotiations between the parties and the transaction was in form a mere sale of tangible assets. *White & Wells v. Commissioner*, 19 B.T.A. 416, Affm'd., 2 Cir. 50 F.(2d) 120; *Pfleggar Hardware Specialty Co. v. Blair*, 2 Cir. (1929), 30 F.(2d) 614; *Betts v. United States*, 62 Ct. Cls. 1; *Didlake v. Roden Grocery Co.*, 160 Ala. 484, 49 So. 384.

C. The testimony of Mr. Grace is entitled to full consideration and weight and the Tax Court erred in disregarding his testimony.

Respondent challenges the testimony of Mr. Grace as being inconsistent with and contrary to the documentary evidence and suggests that little or no weight should be given to his testimony. Respondent's contentions in this regard are not well founded and are not justified by the facts and circumstances.

While it is true that Mr. Grace is an interested party, that is generally true in a tax case and certainly does not disqualify a witness. It should also be noted that Mr. Grace is a man of high standing in the community and has held high office in many business and civil organizations. (R. 20, 47-48.) Respondent's Exhibit M (R. 135) shows that Mr. Grace had made a full statement of the transaction to Government representatives before the trial of this case and that Mr. McFarland, the attorney who represented respondent at the trial had reviewed the statement with Mr. Weller, the representative of Garrett & Company. Mr. McFarland's conference with Mr. Weller apparently disclosed no important discrepancies in Mr. Grace's statement of the transaction for on cross-examination Mr. McFarland did not call attention to any discrepancies between Mr. Grace's testimony and his previous statement. These facts speak well for the accuracy and consistency of the testimony of Mr. Grace.

Despite the fact that the matter was not mentioned on cross-examination respondent now relies on his

Exhibit M (R. 135) in his effort to discredit the testimony of Mr. Grace. (Respondent's Brief, p. 16.) Respondent refers to Mr. Weller's statement that he did not recall that petitioner wanted to sell its plant to Garrett & Company and contends that that statement presents a material contradiction which would justify disregarding other portions of the testimony of Mr. Grace. Respondent omits to mention the preceding sentence in Mr. Weller's statement which reads as follows:

"They (Mr. McFarland and Mr. Tonjes) read me Mr. Grace's statement of the transaction *which was all right* with two exceptions and one was that Mr. Grace claims that when we were dickering he wanted to sell us the winery and made a price of \$125,000 on it but that we insisted that we would prefer a lease." (Italics supplied.) The other exception was that Mr. Weller put petitioner in touch with Taylor Company which purchased the plant in 1944.

Mr. Weller's voluntary statement that Mr. Grace's statement of the transaction, which presumably was the same as his testimony, "was all right" except for the two relatively unimportant exceptions mentioned, would seem to corroborate the testimony of Mr. Grace with regard to the principal elements of the transaction rather than contradict it as respondent contends.

Respondent stresses the fact that the testimony of Mr. Grace that he would not sell anything unless he sold the entire business including the good will is inconsistent with the documentary evidence in which

there is no mention of the good will. Mr. Grace explained that Mr. Weller suggested that he could give him the price asked by paying fifty cents a gallon for the wine. (R. 56.) Since the price was to be computed on the basis of the wine, there was no reason for making further mention of the good will. Respondent states that Mr. Grace could not explain how the good will value was computed in the prices set forth in his telegraphic communication to Garrett & Company in which he suggested varying prices for different wines. On redirect examination Mr. Grace explained that the prices quoted would have given petitioner a little more for its good will than he had asked originally and eventually received and that he thought Garrett & Company might pay the higher price because of the interest they had shown in the previous meetings. (R. 83.) In other words Mr. Grace was merely trying to secure a higher price than that at which he had offered to sell originally.

Respondent asserts that Mr. Grace exaggerated the value and importance of the winery personnel organization and to support this assertion respondent calls attention to Ex. 4-D (R. 121) from which respondent concludes that only \$10,700 was paid by petitioner in 1942 for all wages, salaries and commissions. On the basis of his interpretation of Ex. 4-D respondent asserts that there was "a deliberate effort to color the facts". (Respondent's Brief, p. 20.) While the record does not disclose the salaries which were paid to petitioner's key men and other regular employees, it appears, quite obviously, from an examination of

Ex. 4-D that salaries and other compensation paid in connection with the manufacture of wine were included as part of the Inventory Cost which was \$69,115.82 for the year 1942. There is no basis whatsoever in Ex. 4-D for respondent's conclusions or his accusations.

It is respectfully submitted that respondent's attempts to discredit the testimony of Mr. Grace are based entirely upon misinterpretations and distortions of the evidence. It is further respectfully submitted that the testimony of Mr. Grace is reasonable and logical and when considered in the light of his explanations is not inconsistent with the documentary evidence. Mr. Grace furnished respondent with a statement of the transaction *before* the trial, which was presumably the same as his testimony and that statement when investigated by respondent's attorneys was found to be correct in most material respects by Mr. Weller who represented Garrett & Company in the transaction. The testimony of Mr. Grace was uncontradicted, was in effect corroborated by Mr. Weller's letter (Ex. M, R. 135) and was entitled to full weight and consideration by the Tax Court.

D. In substance and effect the transaction was a sale of petitioner's entire winery business including its good will.

Both the Tax Court and respondent appear to have misunderstood or misinterpreted petitioner's contentions. Petitioner has never contended that it and Garrett & Company entered into an agreement for the sale and purchase of petitioner's good will as such.

Petitioner's contention is that the transaction was in substance and effect a transfer of petitioner's entire winery business and all the assets thereof and since the good will of a business is inseparable from the business, the good will was also transferred even though it was not specifically mentioned in the telegraphic negotiations or the final agreement and even though the purchaser may have had no particular desire for or interest in the good will.

Petitioner owned and operated a successful winery business which had good will of considerable value. Petitioner wanted to dispose of the business but was unwilling to do so except for a price which would be sufficient to compensate it for the tangible assets, which consisted primarily of its wine inventory, and the good will of the business. Petitioner so advised the prospective purchaser and was offered a price for its wine which equalled the total price it would have received for the wine if it had been sold in the regular course of its business plus the price it was asking for its good will.

In the transaction petitioner transferred, by sale and lease, all of the assets of its winery business. Petitioner's entire wine inventory, its plant and equipment, its labels, its list of customers, its staff of experienced employees and its permit to manufacture and sell wine all went over to Garrett & Company. Petitioner retained nothing except the reversionary interest in the plant and equipment which had been leased to Garrett & Company for five years with the

right of renewal. The good will of the business was inseparably attached to the assets which passed to Garrett & Company. Petitioner retained nothing to which the good will could attach. Good will cannot be separated from the business which creates it and it certainly did not remain with the reversionary interest in the plant and equipment.

In *White & Wells Co. v. Commissioner*, 19 B.T.A. 426, Affm'd. 2 Cir., 50 F.(2d) 120 and *Pfleggar Hardware Specialty Co. v. Blair*, 2 Cir., 30 F.(2d) 614, discussed in detail in petitioner's opening brief (pp. 22 to 26), on the basis of facts which were identical in all material respects the Circuit Court for the Second Circuit held that there was a sale of good will. Good will was not mentioned in the sales contracts in either of the cited cases. Likewise the facts establish that the purchasers had no need or desire for the good will of the sellers. In those cases, as here, the Commissioner contended that there had been no sale of good will. The Court held, however, that the good will passed with the other assets of the business and that part of the consideration received was for the good will.

The fact that the purchaser may not have wanted and may never have used the good will is not material. We are here concerned with the seller and its tax liability should be determined on the basis of the consideration it received for the assets it transferred. See *Ida P. Huggins*, 1 T. C. 1214, Pren. Hall, T. C. Memo. Vol. 12, Par. 43172

Perhaps the difficulty with the present case is that good will is an intangible asset which exists only in connection with the business to which it is attached. Suppose that a taxpayer owned and operated a store, with a valuable good will, at a location which was desired by another concern in an entirely different business. If the store owner required the purchaser to buy him out and pay a price which would compensate him for the entire business including the good will, the fact that the purchaser did not want the good will and never made use of it should not have any bearing upon the determination of whether the seller sold his good will or whether part of the consideration received was for the good will.

In the present case petitioner had valuable good will for which it expected to and insisted that it receive compensation. It received the full amount it demanded but in the form of a payment for wine. The fact that the contract recited that the payment was for wine should not change the fact that as far as petitioner was concerned part of the consideration which it received was for its good will.

The evidence establishes that petitioner valued its good will at \$100,000 and included that amount as its price for the good will in determining the total price which was finally received. The record also establishes that the total consideration exceeded the average price at which the wine was being sold in the regular course of business by approximately \$100,000. (R. 60.)

Petitioner respectfully submits that its winery business had a good will value of approximately \$100,000, that in the transfer of all the assets of said business to Garrett & Company, part of the consideration received was allocable to the good will and that the Tax Court erred in failing and refusing to so find.

II.

OTHER ISSUES.

The authorities and arguments with regard to the other issues presented in this appeal are fully presented in petitioner's opening brief (pp. 39 to 46) and no further discussion appears to be necessary.

III.

CONCLUSION.

Petitioner respectfully submits:

(1) That the evidence and authorities cited and discussed in the briefs clearly establish that in the transaction between petitioner and Garrett & Company, petitioner sold its entire winery business including its good will and that at least \$100,000 of the consideration received by petitioner was received by it for its good will.

(2) That since the transaction was a sale of its entire winery business the entire gain constituted long term capital gain and not ordinary income.

(3) That prior to the sale the wine inventory was converted into a capital asset and the gain realized from the sale of the wine (except 4,959 gallons) was long term capital gain and not ordinary income.

Petitioner further respectfully submits that the determination of the Tax Court that the transaction between petitioner and Garrett & Company was merely a sale of wine and barrels and a lease of the winery and that the entire gain constituted ordinary income is clearly erroneous and should be reversed.

Dated, San Francisco, California,
December 15, 1948.

Respectfully submitted,
GEORGE H. KOSTER,
BAYLEY KOHLMEIER,
Attorneys for Petitioner.

No. 11977

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

BARNETT POLLACK,

Appellant,

vs.

**PAUL SAMPSELL, Trustee in Bankruptcy of the Es-
tates of JUDD BRADLEY and OLLIE V. BRAD-
LEY, Bankrupts,**

Appellees.

TRANSCRIPT OF RECORD

**Appeal From the District Court of the United States
for the Southern District of California,
Central Division**

FILED

NOV 4 - 1948

PAUL P. O'BRIEN,
CLERK



No. 11977

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

BARNETT POLLACK,

Appellant,

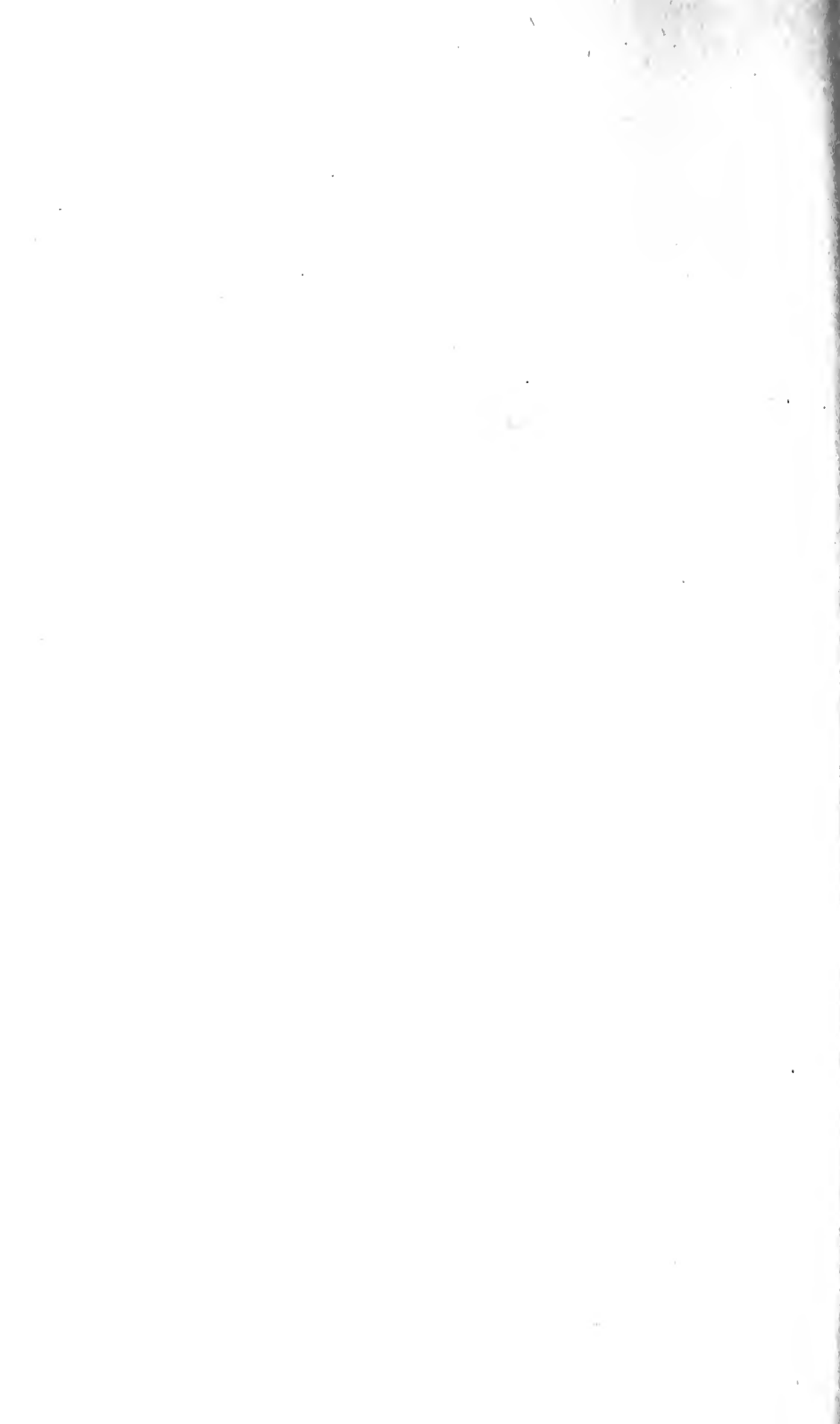
vs.

PAUL SAMPSELL, Trustee in Bankruptcy of the Es-
tates of JUDD BRADLEY and OLLIE V. BRAD-
LEY, Bankrupts,

Appellees.

TRANSCRIPT OF RECORD

Appeal From the District Court of the United States
for the Southern District of California,
Central Division



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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italics; and likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible an omission from the text is indicated by printing in italics the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF ATTORNEYS

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For Appellee:

CRAIG, WELLER AND LAUGHARN

A. R. EARLY, JR.

111 West Seventh Street, Room 817

Los Angeles 14, Calif. [1*]

In the District Court of the United States for the
Southern District of California
Central Division

No. 45333-B

In Proceedings for an Arrangement Under Chapter XI
of the Bankruptcy Act

In the Matter of

JUDD BRADLEY,

Debtor.

PETITION

To the Honorable Judges of the District Court of the
United States in and for the Southern District of
California:

The verified petition of Judd Bradley engaged in the
business of operating a citrus ranch, represents to the
Court as follows:

1. Your petitioner resides at 185 East Jefferson, in
the City of Pomona, County of Los Angeles, State of
California, and has resided at said address for several
years last past.

Your petitioner was and is now engaged in the main-
tenance and operation of a citrus ranch consisting of
one hundred twenty (120) acres located near Lindsay
in the County of Tulare, State of California. Said grove
consists of approximately sixty (60) acres of navel

oranges, forty (40) acres of valencia oranges and twenty (20) acres of cultivatable land with two small houses.

2. Your petitioner has resided within the above judicial district for a longer portion of the six months immediately preceding the filing of this petition than in any other judicial district.

3. Within six (6) years next preceding the filing of this [2] petition, your petitioner has not been known and has not conducted any business by or under any assumed trade or other names or designations.

4. No bankruptcy proceeding initiated by a petition by or against your petitioner is now pending.

5. Your petitioner is unable to pay his debts as they mature.

6. Your petitioner proposes the arrangement with his unsecured creditors, which is annexed hereto and made a part hereof.

7. The Schedule hereto annexed, marked Schedule "A" and verified by your petitioner's oath, contains a full and true statement of all his debts and so far as it is possible to ascertain, the names and places of residence of his creditors and such further statements concerning said debts as are required by the provisions of the Act of Congress relating to Bankruptcy.

8. The Schedule hereto annexed marked Schedule "B" and verified by your petitioner's oath, contains an accurate *an accurate* inventory of all his property, real and

personal, and such further statements concerning said property as are required by the provisions of said Act.

9. Your petitioner has no executory contracts other than the trust deeds against the real estate described in Schedules "A" and "B" herein and the crop mortgage held by the R. M. Anderson packing house.

10. The statement hereto annexed, marked Exhibit 1 and verified by your petitioner's oath, contains a full and true statement of his affairs as required by the provisions of said Act.

Wherefore, your petitioner prays that proceedings may be had upon this petition in accordance with the provisions of Chapter XI of the Act of Congress relating to bankruptcy.

JUDD BRADLEY

Petitioner

CARTER, YOUNG & ZETTERBERG

By Allan J. Carter

Attorneys for Petitioner [3]

[Verified.]

[Endorsed]: Filed Oct. 9, 1947. Edmund L. Smith,
Clerk. [4]

[Title of District Court and Cause]

APPROVAL OF DEBTOR'S PETITION AND ORDER OF REFERENCE UNDER SECTION 322 OF THE BANKRUPTCY ACT

At Los Angeles, in said District, on October 9, 1947, before the said Court the petition of Judd Bradley that he desires to obtain relief under Section 322 of the Bankruptcy Act, and within the true intent and meaning of all the Acts of Congress relating to bankruptcy, having been heard and duly considered, the said petition is hereby approved accordingly.

It is thereupon ordered that said matter be referred to Hubert F. Laugharn, Esq., one of the referees in bankruptcy of this Court, to take such further proceedings therein as are required by said Acts; and that the said Judd Bradley shall attend before said referee on October 16, 1947, and at such times as said referee shall designate, at his office in Los Angeles, California, and shall submit to such orders as may be made by said referee or by this Court relating to said matter.

Witness, the Honorable C. E. Beaumont, Judge of said Court, and the seal thereof, at Los Angeles, in said District, on October 9, 1947.

(Seal)

EDMUND L. SMITH

Clerk

By E. M. Enstrom, Jr.

Deputy Clerk

[Endorsed]: Filed Oct. 9, 1947. Edmund L. Smith, Clerk. [5]

In the District Court of the United States for the
Southern District of California
Central Division

No. 45334-B

In Proceedings for an Arrangement Under Chapter XI
of the Bankruptcy Act

In the Matter of

OLLIE V. BRADLEY,

Debtor.

PETITION

To the Honorable Judges of the District Court of the
United States in and for the Southern District of
California:

The verified petition of Ollie V. Bradley, a housewife,
represents to the Court as follows:

1. Your petitioner resides at 185 East Jefferson, in
the City of Pomona, County of Los Angeles, State of
California, and has resided at said address for several
years last past.

Your petitioner is a housewife and also does some part-
time work in a citrus packing house. She is the wife of
Judd Bradley and owns with him as joint tenants, the
one hundred twenty (120) acres citrus ranch near Lind-
say, California, operated by her said husband since Janu-
ary 29, 1947.

2. Your petitioner has resided within the above judicial district for a longer portion of the six months immediately preceding the filing of this petition than in any other judicial district.

3. Within six (6) years next preceding the filing of this petition, your petitioner has not been known and has not conducted [6] any business by or under any assumed trade or other names or designations.

4. No bankruptcy proceeding initiated by a petition by or against your petitioner is now pending.

5. Your petitioner is unable to pay her debts as they mature.

6. Your petitioner proposes the arrangement with her unsecured creditors, which is annexed hereto and made a part hereof.

7. The Schedule hereto annexed, marked Schedule "A" and verified by your petitioner's oath, contains a full and true statement of all her debts and so far as it is possible to ascertain, the names and places of residence of her creditors and such further statements concerning said debts as are required by the provisions of the Act of Congress relating to Bankruptcy.

8. The Schedule hereto annexed marked Schedule "B" and verified by your petitioner's oath, contains an accurate and full inventory of all her property, real and personal, and such further statements concerning said property as are required by the provisions of said Act.

9. Your petitioner has no executory contracts other than the trust deeds against the real estate described in Schedules "A" and "B" herein and the crop mortgage held by the R. M. Anderson packing house.

10. The statement hereto annexed, marked Exhibit 1 and verified by your petitioner's oath, contains a full and true statement of her affairs as required by the provisions of said Act.

Wherefore, your petitioner prays that proceedings may be had upon this petition in accordance with the provisions of Chapter XI of the Act of Congress relating to bankruptcy.

OLLIE V. BRADLEY

Petitioner

CARTER, YOUNG & ZETTERBERG

By Allan J. Carter

Attorneys for Petitioner [7]

[Verified.]

[Endorsed]: Filed Oct. 9, 1947. Edmund L. Smith,
Clerk. [8]

[Title of District Court and Cause]

APPROVAL OF DEBTOR'S PETITION AND ORDER OF REFERENCE UNDER SECTION 322 OF THE BANKRUPTCY ACT

At Los Angeles, in said District, on October 9, 1947, before the said Court the petition of Ollie V. Bradley that she desires to obtain relief under Section 322 of the Bankruptcy Act, and within the true intent and meaning of all the Acts of Congress relating to bankruptcy, having been heard and duly considered, the said petition is hereby approved accordingly.

It is thereupon ordered that said matter be referred to Hubert F. Laugharn, Esq., one of the referees in bankruptcy of this Court, to take such further proceedings therein as are required by said Acts; and that the said Ollie V. Bradley shall attend before said referee on October 16, 1947 and at such times as said referee shall designate, at his office in Los Angeles, California, and shall submit to such orders as may be made by said referee or by this Court relating to said matter.

Witness, the Honorable C. E. Beaumont, Judge of said Court, and the seal thereof, at Los Angeles, in said District, on October 9, 1947.

(Seal)

EDMUND L. SMITH

Clerk

By E. M. Enstrom, Jr.

Deputy Clerk

[Endorsed]: Filed Oct. 9, 1947. Edmund L. Smith, Clerk. [9]

In the District Court of the United States for the
Southern District of California
Central Division

No. 45333

(In Proceedings for an Arrangement Under Chapter XI
of the Bankruptcy Act)

In the Matter of

JUDD BRADLEY,

Debtor.

PETITION FOR TEMPORARY RESTRAINING
ORDER AND ORDER TO SHOW CAUSE

To the Honorable Judges of the District Court of the
United States in and for the Southern District of
California:

Now comes Judd Bradley, debtor herein, and represents to the Court that on or about July 10, 1947, Barnett Pollack, also known as Barney Pollack, now holding two principal notes of the debtor, filed a three month notice of foreclosure for record in Tulare County and that said three months will expire on October 10, 1947 and that said creditor, Barnett Pollack, unless restrained by this Court, will then proceed to publish a notice of sale on all the real estate and other property secured by two trust deeds on the Tulare County Ranch property held by him, therefore cutting off all rights of all other creditors as well as of the debtor and of the debtor's wife, Ollie V. Bradley.

Your petitioner further represents that Frank Childers has attached farm machinery necessary for the operation

of said citrus ranch, to wit, two pumps used to pump oil and the weed spray machine; and that said property will be sold under the execution of the labor claim of said Frank Childers within the [10] next few days unless restrained by this Court.

That said secured creditors will not be injured by the postponement of said proposed publication of sale and said sales under attachment.

Wherefore your petitioner prays that a temporary restraining order may be entered against each of said creditors, restraining them from taking any further action until this petition and any answers thereto may be heard by this Court and that an order may be entered to show cause why an injunctive order should not be issued against each of said creditors restraining them from proceeding further until the further order of this Court.

JUDD BRADLEY

CARTER, YOUNG & ZETTERBERG

By Allan J. Carter

Attorneys for Petitioner

[Verified.]

[Endorsed]: Filed Oct. 9, 1947. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Jul. 12, 1948. Edmund L. Smith, Clerk. [11]

[Title of District Court and Cause]

ORDER TO SHOW CAUSE WITH TEMPORARY
STAY

At Los Angeles, in said district, on the 9 day of October, 1947:

Upon the annexed Petition of Judd Bradley, the above named debtor, verified the 8th day of October, 1947, from which it clearly appears that the Petitioner will be injured by the loss which will result from the sale of his real estate and personal property under attachment, unless his secured creditor, Barnett Pollack, also known as Barney Pollack, is restrained from advertising for sale the one hundred twenty (120) acre citrus ranch near Lindsay, California, which he is threatening to do on October 10, 1947, and unless Frank Childers is restrained from proceeding with his attachment of the farm machinery necessary for the operation of said ranch, and that such injury will be irreparable because such property, if sold, cannot be redeemed by him and the petitioner will have no redress because of such action on the part of said creditors and that such injury will result to the petitioner and to his unsecured creditors before notice could be served and a hearing had on an application for an order tempor- [12] arily restraining such advertising for sale of the real estate and such sale of the farm machinery under attachment, and that an order should be issued temporarily restraining said Barnett Pollack, also known as Barney Pollack and said Frank Childers from enforcing their said liens upon said real and personal property and no adverse interest having been represented, it is

Ordered that Barnett Pollack, also known as Barney Pollack, and said Frank Childers show cause before me in Room 340, United States Courthouse, Los Angeles, California, on the 16 day of October, 1947, at 10 A. M. o'clock of that day or as soon thereafter as counsel can be heard, why they should not be enjoined and stayed until final decree herein or to the further order of this Court from doing any act or commencing any proceeding to enforce their liens upon the one hundred twenty (120) acre citrus ranch near Lindsay, California, and the farm machinery located thereon, and why this Court should not grant said debtor such other and further relief as is just; and it is further

Ordered that for a period of 7 days from the date hereof, unless otherwise ordered by the Court, Barnett Pollack, also known as Barney Pollack, and Frank Childers be, and they hereby are enjoined and stayed from doing any act or commencing any proceedings to enforce their said liens, and it is further

Ordered that service of copies of this Order and of the petition upon which it is made by delivering the same to Barnett Pollack, also known as Barney Pollack, and Frank Childers on or before the 11 day of October, 1947, shall be deemed good and sufficient service hereof.

HUBERT F. LAUGHARN

Referee in Bankruptcy

Issued this 9 day of October, 1947.

[Endorsed]: Filed Oct. 9, 1947. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Jul. 12, 1948. Edmund L. Smith, Clerk. [13]

In the District Court of the United States for the
Southern District of California
Central Division

No. 45334

In Proceedings for an Arrangement Under Chapter XI
of the Bankruptcy Act

In the Matter of

OLLIE V. BRADLEY,

Debtor.

PETITION FOR TEMPORARY RESTRAINING
ORDER, AND ORDER TO SHOW CAUSE

To the Honorable Judges of the District Court of the
United States in and for the Southern District of
California:

Now comes Ollie V. Bradley, debtor herein, and represents to the Court that on or about July 10, 1947, Barnett Pollack, also known as Barney Pollack, now holding two principal notes of the debtor and her husband's, filed a three month's notice of foreclosure for record in Tulare County and that said three months will expire on October 10, 1947, and that said creditor, Barnett Pollack, unless restrained by this Court, will then proceed to publish a notice of sale on all the real estate and other property secured by two trust deeds on the Tulare County ranch property held by him, therefore cutting off all rights of all other creditors as well as of the debtor and of the debtor's husband, Judd Bradley.

Your petitioner further represents that Frank Childers has attached farm machinery necessary for the operation of said citrus ranch, to wit: two pumps used to pump oil

and the weed spray machine, and that said personal property will be sold under the [14] execution of the labor claim of said Frank Childers within the next few days unless restrained by this Court.

Said secured creditors will not be injured by the postponement of said proposed publication of sale and said sales under attachment.

Wherefore, your petitioner prays that a temporary restraining order may be entered against each of said creditors, restraining them from taking any further action until this petition and any answers thereto may be heard by this court, and that an order may be entered to show cause why an injunctive order should not be issued against each of said creditors restraining them from proceeding further until the further order of this Court.

OLLIE V. BRADLEY

CARTER, YOUNG & ZETTERBERG

By Allan J. Carter

Attorneys for Petitioner

[Verified.]

[Endorsed]: Filed Oct. 9, 1947. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Jul. 12, 1948. Edmund L. Smith, Clerk. [15]

[Title of District Court and Cause]

ORDER TO SHOW CAUSE WITH TEMPORARY
STAY

At Los Angeles, in said district, on the 9 day of October, 1947:

Upon the annexed Petition of Ollie V. Bradley, the above named debtor, verified the 9th day of October, 1947, from which it clearly appears that the Petitioner will be injured by the loss which will result from the sale of her real estate and personal property under attachment, unless her secured creditor, Barnett Pollack, also known as Barney Pollack, is restrained from advertising for sale the one hundred twenty (120) acre citrus ranch near Lindsay, California, which he is threatening to do on October 10, 1947, and unless Frank Childers is restrained from proceeding with his attachment of the farm machinery necessary for the operation of said ranch, and that such injury will be irreparable because such property, if sold, cannot be redeemed by her and the petitioner will have no redress because of such action on the part of said creditors and that such injury will result to the petitioner and to her unsecured creditors before notice could be served and a hearing had on an application for an order temporarily restraining such [16] advertising for sale of the real estate and such sale of the farm machinery under attachment, and that an Order should be issued temporarily restraining said Barnett Pollack, also known as Barney Pollack, and said Frank Childers from enforcing their said liens upon said real and personal property and no adverse interest having been represented, it is

Ordered that Barnett Pollack, also known as Barney Pollack, and said Frank Childers show cause before me

in Room 340, United States Courthouse, Los Angeles, California, on the 16 day of October, 1947, at 10 A. M. o'clock of that day or as soon thereafter as counsel can be heard, why they should not be enjoined and stayed until final decree herein or to the further order of this Court from doing any act or commencing any proceeding to enforce their liens upon the one hundred twenty (120) acre citrus ranch near Lindsay, California, and the farm machinery located thereon, and why this Court should not grant said debtor such other and further relief as is just and it is further

Ordered that for a period of 7 days from the date hereof, unless otherwise ordered by the Court, Barnett Pollack, also known as Barney Pollack, and Frank Childers be, and they hereby are enjoined and stayed from doing any act or commencing any proceedings to enforce their said liens, and it is further

Ordered that service of copies of this Order and of the Petition upon which it is made by delivering the same to Barnett Pollack, also known as Barney Pollack, and Frank Childers on or before the 11 day of October, 1947, shall be deemed good and sufficient service hereof.

HUBERT F. LAUGHARN

Referee in Bankruptcy

Issued this 9 day of October, 1947.

[Endorsed]: Filed Oct. 9, 1947. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Jul. 12, 1948. Edmund L. Smith, Clerk. [17]

[Title of District Court and Cause]

AFFIDAVIT AND OBJECTIONS OF BARNETT
POLLACK TO RESTRAINT AGAINST FORE-
CLOSURE

State of California

County of Los Angeles—ss.

Barnett Pollack, being first duly sworn, deposes and says: That he is the Citee and beneficial owner of Deeds of Trust and Notes involved in the above-entitled proceedings; that heretofore and on April 11, 1946, there were assigned to him, by instrument in writing duly recorded, two certain First Deeds of Trust and Notes, dated January 29, 1946, executed by the above Debtor and her husband, Judd Bradley, affecting the real property presently under foreclosure;

That there is an indebtedness remaining unpaid under said Deeds of Trust and Notes, and presently delinquent, in the sum of Sixty thousand five hundred (\$60,500.00) dollars, together with interest thereon at the rate of five per cent (5%) per annum, payable quarterly, interest due from May 1, 1947.

The debtor became in default of the terms of said Notes and Trust Deeds by having failed to make the payments due thereon, in the following installments and on the following dates, to wit: Twenty-five hundred (\$2500.00) dollars due January [18] 1, 1947; Thirty-five hundred (\$3500.00) dollars due July 1, 1947.

Your affiant has for approximately in excess of twenty (20) years immediately last past been engaged in the business of buying, selling and loaning money upon all types of real property; your affiant is familiar with the

character of the within property, same being an orange ranch.

In the opinion of your affiant, there is no possibility, opportunity, probability or capacity whatsoever upon the part of the debtor to refinance or rehabilitate the subject property or his finances in order to raise any sum of money from the proceeds of the subject property over and above the unpaid secured indebtedness to affiant. This opinion and statement is predicated upon the following facts, amongst other grounds, to wit:

(a) The debtor lost approximately sixty per cent (60%) of his Valencia orange spring crop, due to crop crystallization and lack of proper supervision;

and his predecessors [P.T.R.]

(b) The debtor \wedge have been attempting for the last four or five years to sell this ranch at a profit, but *has* been unable to do so;

(c) Affiant is informed and thereupon alleges that numerous old trees have had to be uprooted, thereby lessening the productive capacity of the grove;

(d) Affiant is informed and thereupon alleges that the Debtor has, in the last few years, increased the loan indebtedness, rather than reduced same;

(e) The value of this grove has steadily decreased, and there are innumerable groves of similar type in the same locale as the instant grove, available for purchase concerning which there is little or no activity of sale at all.

Affiant respectfully represents that the within proceedings, upon the part of the Debtor, are an attempt to evade the just terms of the obligations to affiant, for the purpose of [19] securing the benefit of the November harvest or oranges, thereby exhausting as much income

from the property as possible, without payment of the secured obligations of the Debtor.

The within sale is presently set, pursuant to lawful Notice, on October 31, 1947, at 2 P. M., pursuant to the foreclosure proceeding by the Bank of America as trustee. Any delay of the within proceedings will result in irreparable harm to affiant, because there is every prospect that the within land is constantly depreciating in value, and a delay in the sale, with the consequent delay of affiant's possession, will inevitably lead to loss on sale at foreclosure. Your affiant verily believes, and thereupon alleges, that foreclosure proceedings herein will not produce from the highest possible bidder, the amount of money unpaid to your affiant, to wit: the sum of \$60,500.00. Any delay herein would be unconscionable and without benefit to anybody, with the possible exception of such seizure of assets for conversion to the use of the debtor as may be possible.

Wherefore affiant respectfully prays denial of Debtor's Petition to Stay Sale Proceedings herein.

BARNETT POLLACK

Subscribed and sworn to before me this 16th day of October, 1947.

(Seal)

PETER T. RICE

Notary Public in and for Said County and State

[Endorsed]: Filed Oct. 16, 1947. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Jul. 12, 1948. Edmund L. Smith, Clerk. [20]

[Title of District Court and Cause]

MOTION

(a) To Vacate Restraining Order

(b) To Proceed With Foreclosure Sale

Comes now Barnett Pollack, by his counsel, Peter T. Rice, Esq., and respectfully moves the above Honorable Court, as follows, to wit:

(a) For the order of said court vacating temporary stay heretofore ordered, under the terms of which Barnett Pollack was stayed and enjoined from enforcement of First Trust Deed liens on real property;

(b) For order of court granting Barnett Pollack, and the Bank of America National Trust and Savings Association, as trustee under Deeds of Trust, permission to proceed in enforcement of lien of Trust Deeds, Chattel Mortgages, and Notes, pursuant to the terms thereof.

Said motion is made upon the following grounds:

1. The debtor lost approximately sixty per cent (60%) of the Valencia orange spring crop, due to crop crystallization and lack of proper supervision;

2. The debtor has been attempting for the last four or five years to sell this ranch at a profit, but has been unable to do so; [21]

3. Numerous old trees have had to be uprooted, thereby lessening the productive capacity of the grove;

4. Debtor has, in the last few years, increased the loan indebtedness, rather than reduced same;

5. The value of this grove has steadily decreased, and there are innumerable groves of similar type, in the same

locale as the instant grove, available for purchase, concerning which there is little or no activity of sale at all;

6. The within proceedings upon the part of the Debtor are an attempt to evade the just terms of secured obligations, thereby securing the benefit of as much income from the property as possible, without payment of said obligations.

Said motion further is made upon the testimony adduced on behalf of Barnett Pollack at the time of the within hearing, to wit: October 16, 1947.

PETER T. RICE

Attorney for Barnett Pollack

[Endorsed]: Filed Oct. 16, 1947. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Jul. 12, 1948. Edmund L. Smith, Clerk. [22]

In the District Court of the United States for the
Southern District of California
Central Division

No. 45334-B, No. 45,333-B

In the Matter of

OLLIE V. BRADLEY,
JUDD BRADLEY,

Debtors.

ORDER TO VACATE TEMPORARY STAY AND
GRANTING PERMISSION TO PROCEED
WITH FORECLOSURE

The above entitled cause having come on regularly for hearing this 16th day of October, 1947, before the Hon-

orable Hubert F. Laugharn, Referee of the United States District Court, upon application of Barnett Pollack to vacate temporary stay heretofore granted in these proceedings and for permission to proceed with foreclosure proceedings hereinbefore instituted, and this court having heard evidence, and being fully advised in the premises;

It Is Hereby Ordered as follows:

Temporary stay heretofore issued against Barnett Pollack, his servants, agents and representatives, and the Bank of America National Trust and Savings Association, is hereby vacated;

Barnett Pollack, his agents, servants and representatives, and the Bank of America National Trust and Savings Association, are hereby granted permission to proceed in foreclosure of those two certain Deeds of Trust, dated January 29, 1946, executed by Judd Bradley and Ollie V. Bradley to the Bank of America N. T. & S. A., as trustee, wherein Barnett Pollack is beneficiary, affecting the premises described in said Deeds of Trust, being as follows: [23]

The Southeast 1/4 of the Northwest 1/4 of Section 5 excepting the North 467 feet thereof, in Township 20 S., Range 27 E., Mount Diablo Base and Meridian, in the County of Tulare, State of California,

Also

The East 1/2 of the Southwest 1/4 of Section 5 and the East 495 feet of the Southwest quarter of the Southwest quarter of Section 5, in Township 20 S., Range 27 E., Mount Diablo Base and Meridian, in the County of Tulare, State of California.

together with enforcing any and all proceedings therein as shall be necessary, pursuant to the terms of said Trust Deeds and Notes, said Trust Deeds being recorded in Tulare County, California, as follows: Instrument No. 15863, recorded in Volume 1202, page 103; Instrument No. 15859, recorded in Volume 1202, page 95, together with enforcement of all provisions of Chattel Mortgages, given by the above debtor and her husband, Judd Bradley, affecting the personal property on premises above-described, without any restraint or restriction as to the proceedings upon the part of the said Barnett Pollack, his agents, servants, or representatives, or the Bank of America, National Trust and Savings Association, with the sole and single exception of the following, to wit:

It is ordered that all proceeds from sale herein, over and above that sum of money necessary for payment of lawful costs of foreclosure and expenses permissible under the terms of Chattel Mortgages, Deeds of Trust, and Notes, together with payment of unpaid balance and accumulated interest under said afore-mentioned obligations, be, and all parties hereto are directed that the same [24] shall be, paid to Paul W. Sampsell for and on behalf of the creditors of the *Debtor* herein.

Dated: Dec. 24, 1947.

HUBERT F. LAUGHARN

Referee United States District Court

Received Oct. 16, 1947. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Mar. 11, 1948. Edmund L. Smith, Clerk. [25]

In the District Court of the United States
Southern District of California
Central Division

In Bankruptcy No. 45,333-B

In the Matter of
JUDD BRADLEY,
Debtor.

ORDER TO SHOW CAUSE RE TRUST DEEDS

Upon reading and filing the verified Petition of Paul W. Sampsell, Receiver herein,

It Is Hereby Ordered that the Wagner Realty Company, Barnett Pollack and Dr. F. C. Peirsol appear before the Honorable Hubert F. Laugharn, Referee in Bankruptcy, Room 343 Federal Building, Spring and Temple Streets, Los Angeles, California, on the 10th day of November, 1947, at 2:00 o'clock P. M., then and there to show cause, if any there be, why it should not be adjudged and decreed that they have no right whatsoever in the crops growing upon the real property described in said Petition, and why said receiver should not have such other and further relief as may be proper.

It Is Further Ordered that service of this Order may be made by registered letter.

Dated: November 4, 1947.

HUBERT F. LAUGHARN
Referee in Bankruptcy

[Endorsed]: Filed Nov. 4, 1947. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Mar. 11, 1948. Edmund L. Smith, Clerk. [26]

[Title of District Court and Cause]

OBJECTIONS TO RECEIVER'S ORDER TO SHOW
CAUSE RE TRUST DEED

Comes now Barnett Pollack and files objections to Receiver's Order to Show Cause re attempted severance of crops from real property, upon the following grounds:

1. Said crops are part of the real property, being unsevered and unharvested.

2. The first lien holder, Barnett Pollack, has given notice of election to foreclose and has posted date of foreclosure sale, and sale under foreclosure is ready to proceed.

3. The land by which the deed of trust is secured is of insufficient value to pay the unpaid balance of first trust deed and note.

4. To allow the severance of the crop, in the face of an insufficient security, against the first trust deed holder, Barnett Pollack is to permit an unfair advantage to be taken on behalf of the unsecured creditors and to deprive Barnett Pollack of his property, security and lien of his deed of trust, without just compensation.

Said objections are predicated upon all pleadings and [27] evidence herein presented in the within matter, and in particular, upon the admonition given by the Referee to the debtor that any plan of attempted rehabilitation by the debtor would have to include positive demonstrations of financial resources to the extent of at least Ten thousand (\$10,000) dollars.

Respectfully submitted,

BARNETT POLLACK

POINTS AND AUTHORITIES

The right of a mortgagee (beneficiary under deed of trust) in possession to gather crops growing upon the premises and apply the net proceeds thereof towards the discharge of the indebtedness, is superior to the rights of subsequent creditors and mortgagees.

When the possession has been turned over to a mortgagee, all properties derived from possession of the premises becomes additional security for the indebtedness.

Nelson vs. Bowen, 12 P. 2nd 1083, 124 Cal. App. 662.

Spect vs. Spect, 88 Cal. 437, at page 442.

Following foreclosure sale, a mortgagee and purchaser of the property is entitled to the crop growing on the ground, as against crop mortgagee. This principle does not conform with the rule that a real estate mortgage does not cover growing crops; but when the mortgage is terminated by foreclosure and sale, the purchaser is entitled to the rents, issues and profits of the ground earned during the period of redemption as an incident to the legal and equitable title.

Shintaffer vs. Bank of Italy, 216 Cal. 243, 13 Pac. 2nd 668.

Phillips vs. Pac. Land and Cattle Co., 116 Cal.

[Endorsed]: Filed Nov. 10, 1947. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Mar. 11, 1948. Edmund L. Smith, Clerk. [28]

[Title of District Court and Cause]

STIPULATION AND ORDER APPROVING SAME

Whereas, the above-named debtor has filed a Petition for an arrangement under Chapter XI of the Bankruptcy Act in the above-named Court, and

Whereas, Paul W. Sampsell is the duly appointed, qualified and acting Receiver of the estate of the said debtor, and

Whereas, by an instrument entitled Mortgage of Crops and Marketing Agreement dated the 15th day of May, 1947, Judd Bradley and Ollie V. Bradley, his wife, agreed, among other considerations, to sell and market all crops of valencia oranges and navel oranges then standing, planted or grown, or that might during the year 1947 be grown on the hereinafter described property, through Raymond M. Anderson and Elnora Anderson, his wife, and

Whereas, the Bank of America National Trust & Savings Association, an unsecured creditor of the above-named debtor, through its attorney, and Barnett Pollack, holder of a first trust deed upon the following described real property, through his attorney Peter Rice, [29] have assented in open court to this Stipulation, and

Whereas, the said crop of navel oranges is ready for harvesting and irreparable damage may be sustained by said crop if such harvesting is further delayed,

It Is, Therefore, Stipulated, by and between the said Paul W. Sampsell, as receiver of the estate of the said debtor, and the said Raymond M. Anderson and Elnora Anderson as follows:

Raymond M. Anderson shall immediately harvest the current crop of navel oranges now standing upon the following described real property situated in the County of Tulare, State of California, and for this purpose shall have the right to enter upon said property and do all things thereon required in connection with such harvest, and he shall do all things reasonably necessary to the protection of the crop of navel oranges growing thereon, including smudging the navel orange grove:

The East half of the Southwest quarter ($SW\frac{1}{4}$) of Section Five (5), and the East 495 feet of the Southwest quarter ($SW\frac{1}{4}$) of the Southwest quarter ($SW\frac{1}{4}$) of Section Five (5), in Township Twenty (20) South, Range Twenty-seven (27) East, Mount Diablo Base and Meridian;

The Southeast quarter ($SE\frac{1}{4}$) of the Northwest quarter ($NW\frac{1}{4}$) of Section Five (5), excepting the North 467 feet thereof, in Township Twenty (20) South, Range Twenty-seven (27) East, Mount Diablo Base and Meridian.

Raymond M. Anderson shall haul the said crop from the place of harvesting to his place of business in Lindsay, California. He shall pay the costs incurred in harvesting, hauling, and protecting the said crop, but in the absence of further agreement he shall not be required to advance in excess of \$1,000.00 for the purchase of oil and the hiring of labor for smudging purposes. He shall have the sole and exclusive right to sell and dispose of the said crop and to retain from the proceeds of such sale One Dollar and 15/100 (\$1.15) for all boxes packed, 25/100 Dollars (\$.25) per box handled or processed in the category known as loose fruit, an additional charge of 10/100 Dollars [30] (\$.10) per box on all

oranges that must be processed through the separation machines, plus the actual and necessary expenses incurred in harvesting, protecting and hauling the said crop. The balance of said proceeds shall be paid to the said receiver and the lien upon the said crop claimed under the said Mortgage of Crops of Raymond M. Anderson and Elnora Anderson shall be transferred and attached thereto pending further order of court. Raymond M. Anderson will render to said receiver a full, true and correct account of all sales of said crop showing in detail the amounts received therefor, the expenses of harvesting, protecting, hauling, packing and processing, and the net amount payable to the said receiver.

In Witness Whereof, the said Raymond M. Anderson and Elnora Anderson and the said receiver have hereunto set their hands this 14th day of November, 1947.

RAYMOND M. ANDERSON
ELNORA ANDERSON
PAUL W. SAMPSELL, Receiver

ORDER

It Is Hereby Ordered that the within Stipulation is approved.

Done this 20 day of November, 1947.

HUBERT F. LAUGHARN
Referee in Bankruptcy

[Endorsed]: Filed Nov. 20, 1947. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Mar. 11, 1948. Edmund L. Smith, Clerk. [31]

[Title of District Court and Cause]

OBJECTIONS AND PROPOSED AMENDMENTS
IN RE FINDINGS OF FACT

Comes Now Barnett Pollack, by his counsel, Peter T. Rice, and files herewith objections and proposed amendments in re findings of fact, as submitted by counsel for receiver herein, as follows, to wit:

Said Findings of Fact and Conclusions of Law are deficient in the following respects, to wit:

As to the Findings of Fact the following should be inserted to remedy omissions:

I.

The deeds of trust and notes predicated upon which Barnett Pollack has his first lien were executed January 29, 1946, and assigned to Barnett Pollack on April 11, 1946. A delinquency occurred under the terms of said notes and deeds of trust by the failure of the debtors to pay the Twenty-five hundred (\$2500.00) dollar installment due on January 1, 1947, the Thirty-five hundred (\$3500.00) dollar installment due on July 1, 1947, and all interest installments from May 1, 1947; as a result thereof, Barnett Pollack, as beneficiary, under the terms of said assignment, caused Notice of Election to Declare Default to be filed, said Notice [32] having been recorded July 10, 1947, in Volume 1259, page 337, Official Records of the County of Tulare, California. A sale of all of the real property under the Deed of Trust was regularly scheduled for October 31, 1947, at 2 P. M.

II.

The terms of said Deed of Trust and note provided that the Bank of America, N. T. & S. A., was the trustee;

the debtors deeded said property to said trustee for the benefit of the assignors of Barnett Pollack; said Deed of Trust contains the following provisions:

(1) That the transfer of said real property carried the right, "as additional security to collect the rents, issues and profits thereof."

(2) That upon default by the Trustors (debtors) the Trustee could proceed with sale and foreclosure in the usual manner of foreclosure of Deeds of Trust.

III.

Barnett Pollack filed his written objections to the restraining order and request for leave of court to proceed with foreclosure sale. Following such written protest and request on the part of Barnett Pollack it was shown as follows:

1. The debtors' crops were in a poor and neglected condition;

2. The debtors lost approximately sixty per cent (60%) of Valencia orange spring crop due to crop crystallization and lack of proper supervision;

3. Numerous old trees on grove have to be uprooted, thereby lessening productive capacity of the grove;

4. The indebtedness of the debtors had increased during the preceding years;

5. The value of the grove has steadily decreased;

6. Debtors had no plan of financing for purposes of [33] rehabilitation;

7. Debtors had no finances;

8. The value of debtors' property was steadily decreasing;

9. Debtors had no equity in said real property, capable of financial liquidation.

IV.

The objections of Barnett Pollack against restraining order were overruled and the terms of the restraining order were continued in force and effect, which restraining order did contain, amongst other things, the following: "Barnett Pollack is restrained and enjoined from doing any act or commencing any proceeding to enforce his lien upon the property in question."

V.

That by virtue of said restraint, the sale scheduled for October 31, 1947, at 2 P. M. was continued. At the time scheduled for said sale, to wit: October 31, 1947, at 2 P. M. the Navel crop of oranges was still on the trees and part of the realty.

VI.

The picking of Navel oranges commenced on or about November 15, 1947. But for the restraint against Barnett Pollack and the Bank of America N. T. & S. A. from proceeding with the foreclosure sale of October 31, 1947, Barnett Pollack would have been in possession of the real property, and would, thereupon, have been entitled to harvest the crop of Navel oranges.

VII.

Restraint against foreclosure was lifted by order of court permitting sale to proceed in the regular manner, on January 7, 1948, at 2 P. M. At said sale Barnett Pollack was the sole bidder and purchaser of the real property involved herein; neither the debtors nor anyone

in their behalf appeared or bid at said foreclosure sale. [34]

The following suggestions are presented re Conclusions of Law:

The crop mortgage being declared invalid is invalid for all purposes and cannot be used to deprive the beneficiary Barnett Pollack of any portion of the land and crop affixed thereto, covered by Deed of Trust.

Beneficiary and purchaser under foreclosure sale, Barnett Pollack, should have awarded to him and ordered turned over to him all of the net proceeds available from the sale of Navel crop by Raymond M. Anderson and Elnora Anderson.

All conclusions of law inconsistent with the foregoing are objected to by Barnett Pollack for the reasons aforementioned and for the following reasons:

The debtors, being in the position of having lost their rights to the land, together with all rents, issues and profits thereof, cannot carve from the land an estate, consisting of the crop, by the execution of a void crop mortgage, so as to convey and vest in debtors' creditors an interest in said crop (so to do would be to allow that to be done indirectly which cannot be done directly). As between debtors and beneficiary and purchaser at sale under foreclosure, beneficiary and purchaser at sale is entitled to the land and all rents, issues and profits thereof. To hold otherwise would be to permit any debtor about to lose his crop under foreclosure to execute a

void crop mortgage, apply for relief under Chapter 11, and thereby remove from the realty a crop which was affixed to the realty at the time of the regularly scheduled foreclosure sale and give it to the debtor's creditors at some future crop-picking time after the date of foreclosure. The inequity of this anomalous situation is apparent.

The conclusions of law, further, are predicated upon the erroneous premise as follows: The Conclusions, as presented, state that Barnett Pollack, as beneficiary, is subordinate to the crop [35] mortgage. Then it goes on to say that the crop mortgage is invalid. By such a fiction Barnett Pollack, as the holder of a valid lien by Deed of Trust, is deprived of his security, all under the fiction and facade of a void crop mortgage.

It is respectfully requested, therefore, that the Findings of Fact and Conclusions of Law be amended in accordance with the suggestions, additions and changes herein presented.

Respectfully submitted,

PETER T. RICE

Attorney for Barnett Pollack [36]

[Affidavit of Service by Mail.]

[Endorsed]: Filed Feb. 6, 1948. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Mar. 11, 1948. Edmund L. Smith, Clerk. [37]

[Title of District Court and Cause]

FINDINGS OF FACT, CONCLUSIONS OF LAW
AND ORDER AFTER HEARINGS ON ORDER
TO SHOW CAUSE RE CROP MORTGAGE
AND ORDER TO SHOW CAUSE RE TRUST
DEEDS

The Petition for Order to Show Cause Re Crop Mortgage and the Petition for Order to Show Cause Re Trust Deeds, both filed herein by Paul W. Sampsell as Receiver of the estate of the above-named bankrupt, having regularly come on for hearing before the undersigned Referee in Bankruptcy on the 10th day of November, 1947, and the Receiver herein having appeared in person and by his attorneys Craig & Weller, A. R. Early, Jr. of counsel, and Raymond M. Anderson and Elnora Anderson, his wife, having appeared by their attorney Virgil C. Dowell and by Elnora Anderson, and Dr. F. C. Piersol having appeared in person and Barnett Pollack having appeared in person and by his attorney Peter T. Rice, and no appearance having been made on behalf of the Wagner Realty Company, and both matters having been continued from time to time, a Stipulation having been entered into by the said Receiver, Raymond M. Anderson and Elnora Anderson, and consented to in Open Court by the said Dr. F. C. Piersol and Barnett Pollack and filed herein entitled Stipulation and Order Approving Same authorizing [38] the said Raymond M. Anderson and Elnora Anderson to harvest and sell the crop of navel oranges growing upon the therein described real property, which crop with other property was subject to said crop mortgage and, after deducting certain expenses as set forth in said Stipulation, to pay the bal-

ance of the proceeds of such sale to said Receiver, the lien upon said crop claimed under said crop mortgage to be transferred to said balance pending further order of this Court, testimony having been taken and evidence introduced, and due deliberation had thereon, the Court being fully advised in the premises now makes and enters the following:

FINDINGS OF FACT

I.

The proceedings in bankruptcy herein were commenced by the filing of a Petition under Chapter XI of the Bankruptcy Act on the 9th day of October, 1947. Among the assets of the estate herein were the following parcels of real property situated in Tulare County, California:

The Southeast Quarter (SE $\frac{1}{4}$) of the Northwest Quarter (NW $\frac{1}{4}$) of Section Five (5), excepting the North 467 feet thereof, in Township Twenty (20) South, Range Twenty-Seven (27) East, Mount Diablo Base and Meridian.

II.

Said real property was subject to valid purchase money first trust deeds executed by the bankrupt herein in favor of or assigned to Barnett Pollack as beneficiary. Valid second trust deeds were executed by said bankrupt upon the same property, naming Dr. F. C. Piersol as beneficiary, to secure the repayment of money loaned. All of said deeds of trust conveyed as security the said real

property together with the rents, issues and profits thereof, and were promptly and properly recorded as deeds of trust of real property, but none were entitled on the face thereof apart from and preceding all other [39] terms of the instruments to be mortgages of crops as required by §2956 of the California Civil Code, nor were they recorded as crop mortgages as required by §2957 of said Code.

III.

On or about May 15, 1947, and subsequent to the execution and recordation of said deeds of trust the said Raymond M. Anderson and Elnora Anderson made an unsecured loan of \$12,500.00 to the bankrupt herein for the purpose of discharging a prior crop mortgage held by one W. A. Snyder and/or the Pomona Bank as mortgagees. Between May 15, 1947, and June 14, 1947, the said Raymond M. Anderson and Elnora Anderson made further advances to said bankrupt in the approximate amount of \$3,562.58 for the purpose of discharging current business obligations of said bankrupt. A crop mortgage dated May 15, 1947, naming the said Raymond M. Anderson and his wife Elnora Anderson as mortgagees was signed and acknowledged by the bankrupt herein as mortgagor on August 14, 1947, and by his wife Ollie Bradley on August 28, 1947. Said crop mortgage was given to secure the said loans. Due to the fault of the said bankrupt said mortgage was not delivered to the said mortgagees until September 12, 1947, and was recorded the next day.

IV.

At the time of recording said crop mortgage on September 13, 1947, said bankrupt was insolvent and the said Raymond M. Anderson and Elnora Anderson knew and had reasonable cause to believe that said bankrupt was insolvent. The effect of the execution and recordation of said crop mortgage, if permitted to stand, will be to enable the said Raymond M. Anderson and Elnora Anderson to obtain a greater percentage of their debt than other unsecured creditors of the bankrupt herein.

V.

At the time of the execution of the aforesaid trust deeds and crop mortgage and at all times subsequent thereto until the commencement of the proceedings herein, the bankrupt has been in [40] actual possession of the aforesaid real property.

The trust deeds and notes predicated upon which Barnett Pollack has his first lien were executed January 29, 1946, and assigned to Barnett Pollack on April 11, 1946. A delinquency occurred under the terms of said notes and trust deeds by the failure of the bankrupt to pay the Twenty-Five Hundred Dollars (\$2500.00) installment due on January 1, 1947, and the Thirty-Five Hundred Dollars (\$3500.00) installment due on July 1, 1947, and all interest installments from May 1, 1947. As a result thereof, Barnett Pollack as beneficiary under the terms of said assignment caused a Notice of Election to Declare Default to be filed, said Notice having been recorded July 10, 1947, in Volume 1259, at page 337 of Official Records

of the County of Tulare, California. A sale of all the real property under the trust deed was regularly scheduled for October 31, 1947, at 2:00 o'clock p. m.

Said trust deed and note named the Bank of America National Trust and Savings Association as trustee. The bankrupt deeded said property to said trustee for the benefit of the assignors of Barnett Pollack. Said trust deed contains provisions that the transfer of said real property carried the right "as additional security to collect the rents, issues and profits thereof", and that upon default by the trustor the trustee could proceed with sale and foreclosure.

Upon the representation of the bankrupt and the receiver that there was a marketable equity in the property subject to said trust deeds upon which there could be a net realization over and above the amount owing to the said Barnett Pollack, the Referee issued a restraining order restraining the foreclosure under said trust deed during the pendency of the within proceedings and until January 7, 1948. Barnett Pollack filed a written objection to the restraining order and request for leave of court to proceed with foreclosure sale. Said objections were overruled and the terms of the restraining order were continued in force and effect, which order stated, among other things, "Barnett Pollack is restrained and enjoined from doing any act or commencing any [41] proceeding to enforce his lien upon the property in question". By virtue of said restraint the sale scheduled for October 31, 1947, was continued. At the time scheduled for said sale the crop of navel oranges was still on the trees. The pick-

ing of navel oranges commenced on or about November 15, 1947. But for the restraint against Barnett Pollack and the Bank of America National Trust and Savings Association from proceeding with the foreclosure sale of October 31, 1947, Barnett Pollack would have sold the said real property.

Restraint against foreclosure was lifted by order of court permitting sale to proceed in the regular manner on January 7, 1948, at 2:00 o'clock p. m. Barnett Pollack was the sole bidder at said sale and the purchaser of the real property involved herein. Neither the bankrupt nor anyone on his behalf appeared or bid at said sale.

Based upon the preceding Findings of Fact, the Court makes and enters the following: [42]

CONCLUSIONS OF LAW

I.

The beneficiary of a duly recorded deed of trust conveying real property, together with rents, issues and profits thereof, is not entitled to a crop growing upon that real property as against the trustor or the holder of a subsequent crop mortgage thereon, nor against the receiver or trustee in bankruptcy of the trustor.

II.

The execution of said mortgage constituted a transfer of property of the bankrupt herein to a creditor on account of an antecedent debt. For the purposes of this proceeding §60 of the Bankruptcy Act provides that said transfer shall be deemed to have been made at the time

of recordation of said crop mortgage. Said transfer constituted a voidable preference under said §60.

Based upon the preceding Findings of Fact and Conclusions of Law.

It Is Ordered that the lien of the crop mortgage on certain property of the bankrupt herein executed and delivered by said bankrupt to Raymond M. Anderson and Elnora Anderson and recorded on September 13, 1947, described above be and the same hereby is declared to be void as against the receiver herein and the same hereby is preserved for the benefit of this estate.

It Is Further Ordered that said Raymond M. Anderson and Elnora Anderson within five days of the entry of this Order shall deliver to the said Paul W. Sampsell and shall file with this Court a verified accounting of the harvesting and sale of said crop of navel oranges.

It Is Also Ordered that Barnett Pollack, the Wagner Realty Company and Dr. F. C. Piersol have no right, title or other [43] interest as against the receiver and trustee herein in the said crop of navel oranges, or the proceeds of sale thereof.

Feb. 9, 1948.

HUBERT F. LAUGHARN

Referee in Bankruptcy

Received Feb. 5, 1948. Hubert F. Laugharn, Referee.

[Endorsed]: Filed Mar. 11, 1948. Edmund L. Smith, Clerk. [44]

In the District Court of the United States for the
Southern District of California
Central Division

No. 45,333-B No. 45,334-B

In the Matter of

JUDD BRADLEY and
OLLIE V. BRADLEY,

Debtors.

PETITION FOR REVIEW OF REFEREE'S ORDER
BY JUDGE

To Hubert F. Laugharn and David Head, Referees in
Bankruptcy:

The petition of Barnett Pollack respectfully represents:

I.

Your petitioner is a secured creditor of the above-named bankrupts, by reason of the following: your petitioner is and was the owner of certain first Deeds of Trust and notes executed January 29, 1946, by the debtors, affecting the real property herein concerned, generally described as a 120-acre orange ranch, located in Lindsay, California, the legal description of which real property is more particularly contained in the records on file herein, and which Deeds of Trust and notes, two in number, were purchased by and assigned to the petitioner, on April 11, 1946; said Deeds of Trust and notes were given to secure an indebtedness of the debtors in the unpaid balance of \$60,500.00.

II.

Upon petition of counsel for debtors, a restraining order was issued against petitioner, restraining and enjoin-

ing petitioner "from doing any act or commencing any proceeding to [45] enforce his lien" under said Deeds of Trust. Said Deeds of Trust were on customary trust deed forms, and did contain the following provisions:

(1) That the transfer of said real property carried the right, "as additional security to collect the rents, issues and profits thereof."

(2) That upon default by the Trustors (debtors) the Trustee could proceed with sale and foreclosure in the usual manner of foreclosure of Deeds of Trust.

III.

That prior to restraining order having been issued by the Honorable Referee herein, sale and foreclosure of said Deeds of Trust was regularly scheduled to take place on October 31, 1947, at 2 P. M., by the Trustee named in said Deeds of Trust, to wit: Bank of America, National Trust & Savings Association.

IV.

That on said 31st day of October, 1947, the crop of navel oranges on said property and attached to the trees upon said real property was unpicked and a part of the real property.

V.

Following issuance of Order to Show Cause by Referee, herein described, against your petitioner why restraint should not be issued, petitioner caused to be filed his written objections thereto and his request for leave of court to proceed with foreclosure sale, under provisions of Deeds of Trust aforementioned.

VI.

Thereafter, hearings were had upon debtors' application for restraining order against foreclosure and continued from time to time and restraining order held in force and effect, from time to time, followed by which the Honorable Referee dissolved restraining order herein and permitted foreclosure sale, which was thereafter conducted on Jan. 7, 1948. [46]

VII.

Pending the continuance of restraining order against foreclosure, and following the date upon which foreclosure sale would have regularly taken place (October 31, 1947) had not the restraining order been in force and effect, and on or about November 15, 1947, a navel crop of oranges was commenced to be picked (under the supervision of the Receiver).

VIII.

Thereafter, the Receiver presented his petition for Order to Show Cause why your petitioner should not be adjudged to have no claim whatsoever in said crop of navel oranges; to this, petitioner filed his written objections.

IX.

Following dissolution of restraining order, restraining your petitioner from proceeding with foreclosure, and on February 9, 1948, the Honorable Referee herein did execute his Findings of Fact and Conclusions of Law.

X.

The Conclusions of Law Are Erroneous in the Following Respects and for the Following Reasons:

(a) Regarding Paragraph I of Referee's Conclusions of Law, same presumes the existence of a valid crop

mortgage. The Findings of Fact declare the crop mortgage to be invalid. The Conclusions of Law declared the crop mortgage to be valid solely for the purpose of creating a fictitious estate in the real property in an effort to exempt the fictitious estate (crop mortgage) from the effect of the Deed of Trust, and to allocate the benefit of same for the general creditors. It is respectfully submitted that such a procedure is bringing about indirectly that which is prohibited directly, viz.: permitting a trustor to create an invalid crop mortgage as against a pre-existing First Deed of Trust, so as to give a preference to his general creditors. [47] The Findings of Fact having declared the crop mortgage to be invalid, same is invalid for all purposes and cannot be used to deprive a beneficiary under said Deeds of Trust of any portion of the land or the crops affixed thereto from the beneficial rights of his Deeds of Trust.

(b) The void character of the crop mortgage is attested by Paragraph II of the Referee's Conclusions of Law which declares the crop mortgage void as a preference to the alleged crop mortgagee.

XI.

The Orders of the Referee, Based on Said Findings of Fact and Conclusions of Law, Are Erroneous in the Following Respects and for the Following Reasons:

(a) As respects the order declaring that this petitioner has no right, title or interest against the Receiver and Trustee in the crop of navel oranges or the proceeds thereof; said order is erroneous for the following reasons: it having been declared in the Findings and Conclusions that the crop mortgage was and is invalid, there is no lien, therefore, of legal standing which can void or diminish the effect of the Deeds of Trust and notes held

by petitioner aforementioned. The debtors being in the position of having lost their rights to the land, by reason of default under Deeds of Trust and notes, together with all rents, issues and profits of the land, cannot carve from the land an estate of the debtors, consisting of the crop, by the execution of a void crop mortgage, so as to convey and vest in debtors' creditors an interest in said crop (so to do would be to allow that to be done indirectly which cannot be done directly). As between debtors and petitioner (petitioner also being purchaser at foreclosure sale) petitioner is entitled to the land and all rents, issues and profits thereof, and to the crop growing on the land, as of the date of regularly scheduled sale, [48] to wit: October 31, 1947. To hold otherwise would be to permit any debtor about to lose his crop under foreclosure to execute a void crop mortgage, apply for relief under Chapter XI, and thereby, remove from the realty a crop which was affixed to the realty at the time of the regularly scheduled foreclosure sale and give it to the debtor's creditors at some future crop-picking time after the date of foreclosure. The inequity of this anomalous situation is apparent.

The orders of the Referee are predicated upon the erroneous premise as follows: The Conclusions stated that Barnett Pollack, as beneficiary, is subordinate to the crop mortgage. That it goes on to say that the crop mortgage is invalid. By such a fiction, Barnett Pollack, as the holder of a valid lien by Deed of Trust, is deprived of his security, all under the fiction and facade of a void crop mortgage.

By lifting the restraint against foreclosure, the Referee acknowledged thereby that there was no valid reason to restrain petitioner from proceeding with his rights under

Deeds of Trust and notes. There, therefore, being no reason to have restrained the petitioner, he cannot be made to suffer a loss by a delay, against which he made proper and due objection, against his foreclosure rights, and all of his rights as of October 31, 1947, should be acceded to him. Included in these rights is the right to a crop of oranges growing on the trees on October 31, 1947. To cause petitioner to suffer a loss of this growing crop, solely by reason of a forced delay, based upon a void crop mortgage, is both illegal and inequitable. The purchaser of this property on October 31, 1947, would have taken same free and clear of any claims by general creditors under a void crop mortgage. The same rights should be accorded petitioner, whose sale was delayed against his will, wish and consent and over his written objections. [49]

Wherefore petitioner prays for a review of said Conclusions of Law and Orders of Referee by the Judge, and that the said Conclusions of Law and Orders of the Referee be amended as follows:

As to Conclusions of Law:

1. The beneficiary of a duly recorded Deed of Trust conveying real property, together with rents, issues and profits thereof, is entitled to all of the realty and all growing crops thereon, as against the Trustor or the holder of a void subsequent, crop mortgage thereon, or against the Receiver or Trustee in Bankruptcy of the Trustor.

As to the Orders of the Referee:

1. It is also ordered that there is no lien created against the crop growing or harvested on said real property by virtue of a void crop mortgage.

2. It is also ordered that all of the benefits of the harvest and sale of the crop of navel oranges performed and realized herein be, and they are hereby, awarded to Barnett Pollack, as the holder of the First Deeds of Trust and notes upon said real property, and that Paul W. Sampsell and Raymond M. Anderson and Elnora Anderson have no rights, title or interest therein, except as to permit Raymond M. Anderson and Elnora Anderson to receive such moneys and payments as is provided in Stipulation between the said Andersons and Paul W. Sampsell on file herein.

BARNETT POLLACK

Petitioner

PETER T. RICE

Attorney for Petitioner [50]

POINTS AND AUTHORITIES

The right of a mortgagee (beneficiary under deed of trust) in possession to gather crops growing upon the premises and apply the net proceeds thereof towards the discharge of the indebtedness, is superior to the rights of subsequent creditors and mortgagees.

When the possession has been turned over to a mortgagee, all properties derived from possession of the premises becomes additional security for the indebtedness.

Nelson v. Bowen, 12 P. 2nd 1083, 124 Cal. App. 662.

Spect vs. Spect, 88 Cal. 437, at page 442.

Following foreclosure sale, a mortgagee and purchaser of the property is entitled to the crop growing on the ground, as against crop mortgagee. This principle does not conform with the rule that a real estate mortgage does

not cover growing crops; but when the mortgage is terminated by foreclosure and sale, the purchaser is entitled to the rents, issues and profits of the ground earned during the period of redemption as an incident to the legal and equitable title.

Shintaffer vs. Bank of Italy, 216 Cal. 243, 13 Pac. 2nd 668.

Phillips vs. Pac. Land and Cattle Co., 116 Cal. App. 290. [51]

[Verified.]

[Endorsed]: Filed Feb. 19, 1948. David B. Head, Referee.

[Endorsed]: Filed Feb. 19, 1948. Edmund L. Smith, Clerk. [52]

[Title of District Court and Cause]

REFEREE'S CERTIFICATE ON REVIEW

To the Honorable Campbell E. Beaumont, Judge of the Above-Entitled Court:

The verified Certificate of David B. Head, Referee in Bankruptcy, respectfully shows that:

I.

On the 9th day of February, 1948, an order was made in the within proceedings by Referee Hubert F. Laugharn, my predecessor in office, which provided, in part, that Barnett Pollack had no right, title or interest in and to a crop of navel oranges, or in the proceeds received from the sale thereof, produced upon certain real property of this bankrupt estate; the said Barnett Pollack being the

beneficiary under two trust deeds which were encumbrances upon the said real property which consisted of a grove of navel and valencia orange trees near Lindsay, California.

II.

The within file discloses the fact that proceedings were [53] filed herein on the 9th day of October, 1947, under the provisions of Chapter XI (arrangements) of the Bankruptcy Act. The debtor attempted to effectuate a plan of arrangement with his creditors. However, the plan was never confirmed and on the 18th day of December, 1947, an order of adjudication in bankruptcy was made. In the interim, orders were made by the Referee restraining the foreclosure of the trust deeds of which the said Barnett Pollack was beneficiary. When it appeared that the debtor would not be successful in the arrangement proceedings, the restraining orders were dissolved and foreclosure permitted, the sale under the trust deeds being made on January 7, 1948.

III.

In the interim and prior to the sale, the orange crop was picked, harvested and removed from the property by the trustee herein under a stipulation entered into with Raymond M. Anderson and Elnora Anderson, who claimed an interest in and security upon the said crop by virtue of a crop mortgage, the stipulation providing for an impounding of the net funds in the hands of the said Raymond M. Anderson and Elnora Anderson awaiting the determination in the within proceedings of their interest therein. Thereafter and on the 9th day of February, 1948, Referee Hubert F. Laugharn made a further order herein that the said Raymond M. Anderson and Elnora Anderson, as mortgagees, had no right, title or

interest in and to the said crop of navel oranges or the proceeds derived therefrom by virtue of their alleged chattel mortgage.

IV.

On the 19th day of February, 1948, I granted an extension of time of twenty days within which the said Raymond M. Anderson and Elnora Anderson might file a petition for review from the latter order. The said Raymond M. Anderson and Elnora Anderson have, however, informed the trustee that they do not desire to further controvert the position of the trustee and that further that they will not file such a petition for review. [54] Originally there were three claimants for the funds held by the trustee and received from the sale of the said crop of navel oranges, to-wit: the trustee herein who has been awarded the said proceeds by the said order dated February 9, 1948, the said Barnett Pollack, the petitioner for review of the said order, and Raymond M. Anderson and Elnora Anderson. The order determining that the Andersons have no interest therein having become final, the only remaining contestants for the said fund are the said Barnett Pollack and the said trustee.

V.

Referee Hubert F. Laugharn has made extensive Findings of Fact and Conclusions of Law upon the said order. There does not appear to be a dispute upon the facts in this controversy, the same involving a point of law for determination herein.

The question presented is:

1. Does Pollack have any right, title, interest or lien upon the navel orange crop which was removed and converted into cash prior to the trust deed foreclosure sale? The Referee answered this question in the negative.

There is attached hereto and forwarded herewith the following:

1. Petition for Temporary Restraining Order.
2. Order Restraining Harvesting of Orange Crop.
3. Receiver's Petition for Order to Show Cause re Trust Deeds.
4. Order to Show Cause re Trust Deeds dated November 4, 1947.
5. Memorandum of Points and Authorities (Receiver's).
6. Barnett Pollack's Objections to Receiver's Order to Show Cause re Trust Deeds.
7. Stipulation and Order Approving Same.
8. Order to Vacate Temporary Stay and Granting Permission [55] to Proceed with Foreclosure.
9. Barnett Pollack's Objections and Proposed Amendments in re Findings of Fact.
10. Findings of Fact, Conclusions of Law and Order after Hearing on Order to Show Cause re Crop Mortgage and Order to Show Cause re Trust Deeds.
11. Petition for Review of Referee's Order by Judge.
12. Trustee's Memorandum of Points and Authorities on Review.

Bankrupts' Voluntary petitions and schedules and orders of Adjudication (by reference).

Dated: March 11, 1948.

Respectfully submitted,

DAVID B. HEAD

Referee in Bankruptcy

[Endorsed]: Filed Mar. 11, 1948. Edmund L. Smith, Clerk. [56]

[Title of District Court and Cause]

NOTICE OF MOTION

To Craig & Weller, and A. R. Early, Jr., Attorneys for
Paul Sampsell, Trustee:

You Will Please Take Notice that Barnett Pollack, petitioner for review of Referee's Order herein, by his counsel, Peter T. Rice, will move the above Honorable Court, the Honorable Campbell E. Beaumont, Judge presiding therein, on Monday, the 5th day of April at 10 A. M. thereof, or as soon thereafter as counsel can be heard, for the review by said Honorable Court of the order of Referee Hubert F. Laugharn, heretofore made and entered, and the substitution in place thereof of an order to the following effect:

That Barnett Pollack, beneficiary under Deeds of Trust, is entitled to all growing crops on the realty covered by said Deeds of Trust, and to the proceeds of said growing crop which was removed under the supervision of the Trustee in bankruptcy, [57] following the regularly scheduled date of sale, to wit: October 31, 1947.

Said motion will be made upon this notice, all records and pleadings on file herein, and will be based upon the grounds set forth in the Objections, Amendments to Conclusions of Law, Points and Authorities set forth in Barnett Pollack's pleadings on file herein, together with further Points and Authorities to be filed by petitioner herein.

PETER T. RICE

Attorney for Barnett Pollack [58]

[Affidavit of Service by Mail.]

[Endorsed]: Filed Mar. 22, 1948. Edmund L. Smith,
Clerk. [59]

[Title of District Court and Cause]

SUPPLEMENT TO REFEREE'S CERTIFICATE ON
REVIEW

To the Honorable Leon R. Yankwich, Judge of the United
States District Court for the Southern District of
California, Central Division:

There has been requested herein that the following documents be added to the Referee's Certificate filed herein on March 11, 1948:

1. Petition for Temporary Restraining Order and Order to Show Cause (Judd Bradley Estate).
2. Order to Show Cause with Temporary Stay.
3. Petition for Temporary Restraining Order, and Order to Show Cause (Ollie V. Bradley Estate).
4. Order to Show Cause with Temporary Stay.
5. Affidavit and Objections of Barnett Pollack to Restraint against Foreclosure (Ollie V. Bradley Estate).
6. Motion: (a) To Vacate Restraining Order; (b) To Proceed with Foreclosure Sale.

Dated: July 12, 1948.

Respectfully submitted,

DAVID B. HEAD

Referee in Bankruptcy

[Endorsed]: Filed Jul. 12, 1948. Edmund L. Smith,
Clerk. [60]

In the District Court of the United States
Southern District of California
Central Division

In Bankruptcy No. 45,333-B

In Bankruptcy No. 45,334-B

In the Matters of

JUDD BRADLEY and

OLLIE V. BRADLEY,

Bankrupts.

ORDER AFTER HEARING ON REVIEW

The Petition for Review of the Referee's Findings of Fact, Conclusions of Law and Order After Hearing on Order to Show Cause Re Crop Mortgage and Order to Show Cause Re Trust Deeds Dated February 9, 1948, Upon the Order to Show Cause Re Trust Deeds, having regularly come on for hearing before the undersigned Judge of the above entitled Court on the 10th day of May, 1948, and Barnett Pollack, the appellant herein, having appeared by his attorney, Peter T. Rice, and Paul W. Sampsell as Trustee in Bankruptcy of the estate of the above named bankrupts, the respondent herein, having appeared by his attorneys, Craig & Weller, A. R. Early, Jr., of counsel, and argument having been heard, the Court now rules upon said petition as follows:

The said Order of the Referee dated February 9, 1948, is affirmed.

Done at Los Angeles in said Southern District of California, this 2nd day of June, 1948.

LEON R. YANKWICH

Judge

Approved as to Form in Accordance With Local Rule 5:
Peter T. Rice, Attorney for Barnett Pollack.

Order entered Jun 2, 1948. Docketed Jun. 2, 1948. C. O. Book 51, page 102. Edmund L. Smith, Clerk; by John A. Childress, Deputy.

[Endorsed]: Filed Jun. 2, 1948. Edmund L. Smith, Clerk. [61]

[Title of District Court and Cause]

NOTICE OF APPEAL

To Paul Sampsell, Trustee in Bankruptcy for the above-named Bankrupts, and to Craig & Weller, His Attorneys:

You and Each of You Will Please Take Notice that Barnett Pollack gives Notice of Appeal, and does hereby appeal to the Ninth Circuit Court of Appeals, from the order dated May 10, 1948, of Judge Leon R. Yankwich, Southern District of California, Central Division, which order affirms the order of Referee, dated February 9, 1948, affecting Findings of Fact and Conclusions of Law and Order after hearing on Order to Show Cause re crop mortgage and Order to Show Cause re trust deeds; said Order affects the disputed claim between the Trustee in bankruptcy and Barnett Pollack, a secured creditor, concerning the right to the financial proceeds of a crop growing on the real property covered by the Deeds of Trust, of said secured creditor.

PETER T. RICE

Attorney for Barnett Pollack, Appellant

[Endorsed]: Filed & mld. copy to Craig, Weller & Laugharn, Attys. for Trustee, Jun. 8, 1948. Edmund L. Smith, Clerk. [62]

[Title of District Court and Cause] .

DESIGNATION OF PORTION OF RECORD
POINTS ON APPEAL

To the Above Honorable Court and to Messrs. Craig & Weller, Attorneys for Paul W. Sampsell, Trustee in Bankruptcy:

You Will Please Take Notice that appellant, Barnett Pollack, herewith designates portion of record, and points upon which appellant relies.

Designation of Portion of Record:

* * * * *

The Points upon which appellant relies are as follows:

1. Barnett Pollack was entitled to all the real property covered by his Deeds of Trust and notes, as of the date upon which his foreclosure sale was regularly scheduled, to wit: October 31, 1947, which includes growing crops thereon existing.

2. The unsevered growing crop of oranges on this realty was a part of the realty to which Barnett Pollack was entitled as of October 31, 1947.

3. The bankrupts, simply by proceeding under the Bankruptcy Act, could not lawfully defeat the right of Barnett Pollack to the realty and all growing crops thereon, as of October 31, 1947.

4. The right to the crop growing on the realty became fixed and vested in equity, and hence at law, as of October 31, 1947. [64]

5. The Trustee, succeeding only to the rights of the bankrupts, cannot, by interposing the aid of the court's restraining order, enlarge upon the title he received from the bankrupts.

6. It is inequitable to deprive the trust deed lien holder of his security by indirect means (the resulting effect of the restraining order) when such rights are denied to the bankrupt directly.

7. The Bankruptcy Act is not intended to defeat rights which vested by operation of law. Under the right of law, Barnett Pollack was entitled to have held a sale of the real property and crops growing thereon as of October 31, 1947. The enforced delay of sale and the interim harvesting of crops does not deny the legal and equitable right of Pollack to his full security as of the time he could have exercised his rights of foreclosure on October 31, 1947.

.....
Attorney for Appellant Barnett Pollack [65]

[Affidavit of Service by Mail.]

[Endorsed]: Filed Jun. 11, 1948. Edmund L. Smith, Clerk. [66]

[Title of District Court and Cause]

NARRATIVE STATEMENT ON APPEAL

Come now counsel for Barnett Pollack, appellant, and Paul W. Sampsell, Trustee, and present narrative statement on appeal herein.

Jurisdiction for the consideration of the within appeal by this court is conferred by Section 24(a) Bankruptcy Act.

Statement of facts and pleadings involved is as follows:

Barnett Pollack is a secured creditor of the above-named bankrupts by virtue of being the owner and holder of certain first Deeds of Trust and notes executed January 29, 1946, by the debtors, affecting the real property herein concerned, generally described as a 120 acre orange ranch, located in Lindsay, California. The bona fide character and status as holder in due course of the said Barnett Pollack is admitted. The unpaid balance on said Deeds of Trust and notes as of the date of the foreclosure herein was Sixty thousand five hundred (\$60,500.00) dollars. By reason of the default of the debtors of principal as follows: due January 1, 1947, Twenty-five hundred (\$2500.00) dollars; July 1, 1947, Thirty-five hundred (\$3500.00) dollars, [67] and interest due from May 1, 1947, foreclosure proceedings of Deeds of Trust, pursuant to California law, were regularly commenced, prior to institution of Chapter XI or Bankruptcy applications.

Following posting of notice of sale and prior to date of sale, the debtors filed proceedings for arrangement under Chapter XI of the Bankruptcy Act. Hearings were

thereupon had from time to time, and provisional orders entered delaying foreclosure sale from time to time. No reviews nor appeals were taken from any of these provisional orders.

On October 31, 1947, the regularly scheduled date of foreclosure sale, the crop of oranges herein concerned was not yet harvested nor ready for harvesting, and was still a part of the realty and on the trees.

On or about November 15, 1947, by order of the Referee in bankruptcy, the crop of oranges was harvested, with the cash proceeds thereof to be paid to the then receiver (present trustee) in bankruptcy, and ordered held until further order of court.

Thereafter, restraint against foreclosure was lifted and foreclosure sale was held on January 7, 1948.

No plan of arrangement or financial rehabilitation was approved by the Referee in bankruptcy, and debtors filed voluntary petition for bankruptcy.

Findings of Fact and Conclusions of Law, together with proposed amendment to Findings of Fact and Conclusions of Law, offered by counsel for appellant, were submitted to the Referee in bankruptcy, and subsequently, signed, as amended in some details, and as revealed by the Findings and Conclusions on file herein. Appellant caused Petition for Review to be presented before the Honorable Leon R. Yankwich, which Honorable Court did, on May 10, 1948, enter its order upholding Findings of Fact and Conclusions of Law of said Referee.

The appeal herein is from the Conclusions of Law. [68]

The questions raised herein are as follows:

1. Are unsevered growing crops a part of the realty, so as to go with the realty as of the date of regularly scheduled foreclosure sale, to wit: October 31, 1947?

2. Can a Referee in bankruptcy cause to bring about a situation wherein an unsecured creditor (Barnett Pollack) can be made to suffer the loss of part of his security by reason of staying a foreclosure sale beyond the date upon which a crop was to be harvested, where such order staying sale was protested by said creditor?

The points upon which appellant relies are as follows:

1. Barnett Pollack was entitled to all the real property covered by his Deeds of Trust and notes, as of the date upon which his foreclosure sale was regularly scheduled, to wit: October 31, 1947, which includes growing crops thereon existing.

2. The unsevered growing crop of oranges on this realty was a part of the realty to which Barnett Pollack was entitled as of October 31, 1947.

3. The bankrupts, simply by proceeding under the Bankruptcy Act, could not lawfully defeat the right of Barnett Pollack to the realty and all growing crops thereon, as of October 31, 1947.

4. The right to the crop growing on the realty became fixed and vested in equity, and hence at law, as of October 31, 1947.

5. The Trustee, succeeding only to the rights of the bankrupts, cannot, by interposing the aid of the court's restraining order, enlarge upon the title he received from the bankrupts.

6. It is inequitable to deprive the trust deed lien holder of his security by indirect means (the resulting effect of the restraining order) when such rights are denied to the [69] bankrupt directly.

7. The Bankruptcy Act is not intended to defeat rights which vested by operation of law. Under the right of law, Barnett Pollack was entitled to have held a sale of the real property and crops growing thereon as of October 31, 1947. The enforced delay of sale and the interim harvesting of crops does not deny the legal and equitable right of Pollack to his full security as of the time he could have exercised his rights of foreclosure on October 31, 1947.

The foregoing narrative is approved as a statement of the case on appeal by respondent, trustee in bankruptcy, but such stipulation makes no admission as to the merit or justice of appellant's appeal.

Respectfully submitted,

PETER T. RICE

Attorney for Appellant

CRAIG & WELLER

By Thomas S. Tobin

Attorney for Respondent Trustee in Bankruptcy

[Endorsed]: Filed Jul. 10, 1948. Edmund L. Smith,
Clerk. [70]

[Title of District Court and Cause]

CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the District Court of the United States for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 72, inclusive, contain full, true and correct copies of Debtor's Petition Under Chapter XI of the Bankruptcy Act and Approval of Debtor's Petition and Order of Reference Under Section 322 of the Bankruptcy Act in each of the above-entitled matters; Debtor's Petition for Temporary Restraining Order and Order to Show Cause and Order to Show Cause with Temporary Stay in each of the above-entitled matters; Affidavit and Objections of Barnett Pollack to Restraint Against Foreclosure in matter No. 45334; Motion to Vacate Restraining Order and to Proceed with Foreclosure Sale in matter No. 45334; Order to Vacate Temporary Stay and Granting Permission to Proceed with Foreclosure; Order to Show Cause re Trust Deeds; Objections to Receiver's Order to Show Cause re Trust Deed; Stipulation and Order Approving same; Objections and Proposed Amendments in re Findings of Fact; Findings of Fact, Conclusions of Law and Order After Hearings on Order to Show Cause re Crop Mortgage and Order to Show Cause re Trust Deeds; Petition for Review of Referee's Order by Judge; Referee's Certificate on Review; Notice of Motion; Supplement to Referee's Certificate on Review; Order After Hearing on Review; Notice of Appeal; Designation of Portion of Record and Statement of Points on Appeal; Nar-

rative Statement on Appeal and Amendment to Designation of Portion of Record on Appeal which constitute the record on appeal to the United States Circuit Court of Appeals for the Ninth Circuit.

I further certify that my fees for preparing, comparing, correcting, and certifying the foregoing record amount to \$15.50 which sum has been paid to me by appellant.

Witness my hand and the seal of said District Court this 15 day of July, A. D. 1948.

(Seal)

EDMUND L. SMITH

Clerk

By Theodore Hocke

Chief Deputy

[Endorsed]: No. 11977. United States Court of Appeals for the Ninth Circuit. Barnett Pollack, Appellant, vs. Paul Sampsell, Trustee in Bankruptcy of the Estates of Judd Bradley and Ollie V. Bradley, Bankrupts, Appellees. Transcript of Record. Appeal From the District Court of the United States for the Southern District of California, Central Division.

Filed July 16, 1948.

PAUL P. O'BRIEN

Clerk of the United States Court of Appeals for the Ninth Circuit

United States Circuit Court of Appeals

Ninth Circuit

No. 11977

BARNETT POLLACK,

Appellant,

vs.

PAUL W. SAMPSELL, Trustee for JUDD BRAD-
LEY and OLLIE V. BRADLEY, Bankrupts,
Respondent.

STATEMENT OF POINTS ON APPEAL

Comes now appellant, by his counsel, Peter T. Rice, and respectfully designates the following Statement of Points on Appeal:

1. Bankruptcy Courts are governed by the principles of equity and the law of the State with respect to right of ownership in crops growing on land which is subject to Deed of Trust.

2. It is inequitable to deprive a Trust Deed lien holder of his security by the indirect method of bankruptcy, when such deprivation is not within the direct power of the debtor.

PETER T. RICE

Attorney for Appellant

[Affidavit of Service by Mail.]

[Endorsed]: Filed Oct. 5, 1948. Paul P. O'Brien,
Clerk.

No. 11977

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

BARNETT POLLACK,

Appellant,

vs.

PAUL SAMPSELL, Trustee in Bankruptcy of the Estates of
JUDD BRADLEY and OLLIE V. BRADLEY, Bankrupts,

Appellees.

APPELLANT'S OPENING BRIEF.

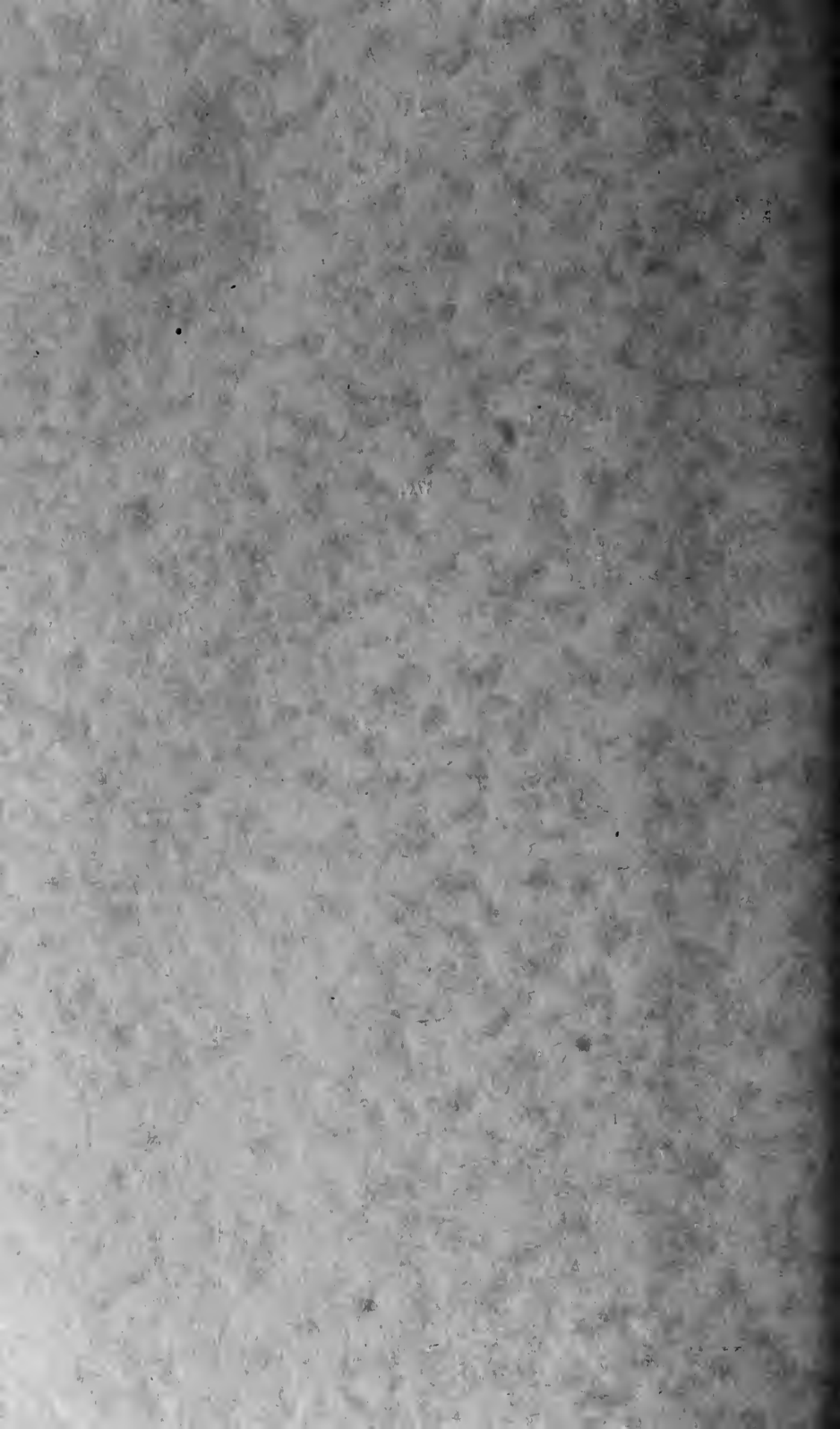
PETER T. RICE,

521 Chester Williams Building, Los Angeles 13,

Attorney for Appellant.

NOV 10 1948

FRANK P. O'BRIEN,



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No. 11977

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

BARNETT POLLACK,

Appellant,

vs.

PAUL SAMPSELL, Trustee in Bankruptcy of the Estates of
JUDD BRADLEY and OLLIE V. BRADLEY, Bankrupts,

Appellees.

APPELLANT'S OPENING BRIEF.

Facts.

This case involves the following question of fact. Appellant was the holder of two First Deeds of Trust upon a ranch owned by the bankrupt. He gave notice of default and time and place of foreclosure sale prior to debtor's insolvency proceeding. Thereafter, such insolvency proceedings were commenced and a restraining order issued which prevented appellant from holding his foreclosure sale upon the date regularly set, to wit: October 31, 1947. Because of such continued restraint, the foreclosure sale was postponed from time to time over objections of Trust Deed holder.

While such restraint was in force, on November 15, 1947, the Trustee harvested a crop of oranges from the

trees growing on the property covered by the Deeds of Trust; the money realized from the sale of such oranges was placed in the general funds of this estate. Following such harvest and sale of crop, appellant was permitted to proceed with his foreclosure sale, which resulted in a deficiency in excess of the amount for which the crop of oranges had been sold. By order of the Referee and of the District Court, appellant was denied the amount which had been secured from the sale of the oranges, and the same was placed in the general assets of the estate for unsecured creditors.

Question of Law.

The sole question of law involved in this appeal is whether the referee in bankruptcy may enjoin a preferred creditor from proceeding with his foreclosure sale, and during the period of such restraint remove portions of the realty, sell the same, and place the proceeds in the general funds of the estate, so as to deprive the preferred creditor of the benefit thereof.

ARGUMENT.

At the outset, it should be noted that had appellant here been permitted to proceed with his regularly noticed foreclosure sale on October 31, 1947, the unripe unharvested oranges, being unquestionably a part of the realty, would have passed with the realty upon sale thereof; and that, to the extent of their value, such sale would have brought an increased amount to be applied to the secured obligation. When the Referee issued the restraining order which prevented the sale, he, in effect, by continuing the restraining order until such time as the crop could be harvested, took from the secured creditor a portion of his security and gave the benefit thereof to another group of creditors, to wit: the unsecured general creditors. The question here involved is whether the Referee may, by restraining order, in effect, prefer one group of creditors over another.

A thorough search of authorities reveals to appellant no case in which this precise point has been before this or any other court, although it would seem the situation could arise upon many occasions. We are, therefore, forced to draw an analogy from cases in which situations did arise which, by implication at least, bear upon the matter now before this court.

1. **Bankruptcy Courts Are Governed by the Principles of Equity and the Law of the State With Respect to Right of Ownership in Crops Growing on Land Which Is Subject to Deed of Trust.**

Bankruptcy courts are governed by the principles of equity. The whole purpose of the Bankruptcy Act is to protect against preferences and frauds and not to defraud one who, in good faith, had advanced or loaned money or security to one who was insolvent at the time. (Note: In our case, it is admitted that there was no element of insolvency at the time the Deeds of Trust were executed, and even if there were, that element would be immaterial in view of same being purchase money Deeds of Trust.

First National Bank v. Livestock National Bank,
31 F. 2d 416.

The matter is well settled that the Referee may, in the exercise of his jurisdiction, issue restraints even as against secured creditors, for the purpose of determining whether there exists any equity in the bankrupt. But it should, however, be noted that jurisdiction exists to restrain mortgagees (secured creditors) only for a reasonable time, and such restraints do not operate to deprive mortgagee (secured creditor) of their security. In the instant case, it is appellant's contention that the interpretation of the order of the Referee is erroneous in that such interpretations:

- (1) Deprives the mortgagee of his security, and
- (2) It is inequitable.

First Trust Co. v. Baylor, 1 F. 2d 24.

The respondent in the court below makes no claim that if foreclosure sale had taken place prior to harvesting of crops that the unharvested crops would not have gone with the land. Respondent concedes that such unharvested crops would have gone with the land on foreclosure sale.

The laws of the State of California would govern the bankruptcy court in respect to the rights and liabilities affecting the orange crop and the land under the deeds of trust.

Bankruptcy courts are governed by the law of the state wherein the lien is created.

First Nat. Bank v. Livestock Nat. Bank, 31 F. 2d 416;

Hyde Park etc. v. West Norwood, 127 F. 2d 654;

In re American Fuel & Power, 151 F. 2d 479.

Unsevered growing crops are a part of the realty in California.

Penryn Co. v. Sherman Worrell Co., 142 Cal. 643;

List v. Sandel, 42 Cal. App. 2d 507;

Cook v. Huntley, 44 Cal. App. 2d 640;

Bank of America v. Hirsch, 64 Cal. App. 2d 184;

Silveira v. Ohm, 189 P. 2d 782.

The title to crops growing on land subject to a Deed of Trust relates back to the date of the giving of the Deed of Trust.

Cook v. Huntley, *supra*;

Bank of America v. Hirsch, *supra*.

2. **It Is Inequitable to Deprive a Trust Deed Lien Holder of His Security by the Indirect Method of Bankruptcy When Such Deprivation Is Not Within the Direct Power of the Debtor.**

We shall not attempt to argue that PRIOR to foreclosure a mortgagor (debtor) is not entitled to the rents, issues and profits of the realty; nor that, as a consequence of this rule, if the mortgagor (debtor) removes a crop from the land prior to sale by the mortgagee (secured creditor) that such sale, or the proceeds therefrom, would not belong to the Trustee in Bankruptcy. We do, however, contend that where a sale is regularly scheduled by the mortgagee (secured creditor) which sale, in the ordinary course of events, would take place prior to the harvesting of the crop, but is prevented by order of court until such time as the crops are harvested, that this is a withholding from the mortgagee (secured creditor) of a portion of his security. This position is further supported by the fact that the courts have repeatedly held that if the value of the security is less than the delinquency, a Trustee should not interfere in the foreclosure thereof.

Issacs v. Howes, 51 S. Ct. 270, 282 U. S. 734;

17 *Am. Bankruptcy Reports* (New Series) 273.

In a note in 75 L. Ed. on the above case, page 668, we find the following statement:

“Where the mortgagee is, under his agreement with the mortgagor, entitled to the possession of a mortgaged crop, he is entitled to such possession, as against the Trustee.”

In the instant case, regardless of whether the Trust Deeds themselves contained a right to take possession or not, it unquestionably gave to the holder of the Trust Deeds the right to have the property sold on the date which he set, in this case, October 31, 1947. We contend that upon that date the holder of the Trust Deed became entitled to the possession of the property, or in the alternative, to hold his sale, and he, therefore, became entitled to such possession, as against the Trustee. Being entitled to such possession, the trust deed holder was entitled to the incidents and appurtenances of the realty. In this case, the unharvested crops of oranges is such an appurtenance. It, therefore, follows that when the Trustee sold the oranges, the Trust Deed holder became entitled to their value and was entitled to follow the fund into the hands of the Trustee.

Gibson v. Warden, 14 Wall. (U. S.) 244, 20 L. Ed. 797.

Appellant believes that if the action of the lower court is upheld, it would, as a practical matter, permit a bankruptcy court, in cases where crops may be harvested, to issue an injunction against the secured creditors' foreclosure for an indefinite period of time. The end purpose of such an order could allow successive crops to be harvested and sold until such time as sufficient funds have been realized to pay off all the unsecured creditors in full, thereby, in effect, making a secured creditor pay unsecured creditors.

If the action of the Referee in bankruptcy is upheld, it means that by filing a petition in bankruptcy, the debtor has placed a secured creditor in a worse position than that which he held prior to the bankruptcy, a situation not con-

templated by the Bankruptcy Act and not sanctioned by the courts.

In *Eyster v. Goff*, 91 U. S. 521, 23 L. Ed. 403, the court stated that the creditor of a bankrupt or the man who contests the right to real or personal property with him loses none of those rights by the bankruptcy of his adversary. The bankrupt is not permitted to enlarge his estate at the expense of the secured creditor. If bankruptcy could be used as a scythe to cut away the security of the trust deed holder, then would not this allow the bankrupt to do indirectly what he could not have done directly?

Conclusion.

In conclusion, while a restraint may be placed upon a secured creditor, preventing him from foreclosing his security, we state that such restraint does not operate to place such creditor in a worse position than he occupied before and that if any of the security be removed or harvested after the date when such creditor is regularly entitled to his foreclosure, such crop or harvest must equitably follow the realty and must be set aside as a fund for the benefit of such secured creditor.

We, therefore, respectfully urge this court to reverse the judgment of the lower court, with instructions that all of the proceeds resulting from sale of the orange crop, less costs of harvesting the same, be declared to be a portion of the security belonging to Barnett Pollack; that such fund be delivered to him by the Trustee in bankruptcy.

Respectfully submitted,

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No. 11977
IN THE
United States Court of Appeals
FOR THE NINTH CIRCUIT

BARNETT POLLACK,

Appellant,

vs.

PAUL W. SAMPSELL, Trustee in Bankruptcy of the Estates
of JUDD BRADLEY and OLLIE V. BRADLEY, Bankrupts,

Appellee.

BRIEF FOR APPELLEE.

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BRIEF FOR APPELLEE.

Jurisdictional Statement.

These bankruptcies were commenced on October 9, 1947, in the District Court of the United States for the Southern District of California, Central Division, by the filing by Judd Bradley and Ollie V. Bradley, husband and wife, of petitions under Section 322 of Chapter XI of the Bankruptcy Act (11 U. S. C. Section 722) for arrangements between themselves and their creditors [Tr. pp. 2 and 6]. Thereafter, the District Court approved the petitions and referred the matters generally to one of the referees in bankruptcy of that court [Tr. pp. 5 and 9]. On October 30, 1947, a receiver was appointed for both estates. The debtors' proposed plans of arrangement were never confirmed and orders of adjudication in bankruptcy were entered on December 18, 1947.

This appeal is from an order of the District Court affirming an order of the referee dated February 9, 1948.

Exclusive jurisdiction of proceedings in bankruptcy is vested in the District Courts of the United States (Bankruptcy Act, Section 2, 11 U. S. C. Section 11) and the Courts of Appeals of the United States are vested with appellate jurisdiction thereof (Bankruptcy Act, Section 24, 11 U. S. C. Section 47).

Statement of the Case.

Among the assets of these bankrupt estates was certain real property subject to valid purchase money trust deeds which conveyed the realty together with the rents, issues and profits thereof to the appellant as security for the payment of certain notes. Orange trees grew upon this real property, but none of the trust deeds were entitled or recorded as crop mortgages [Tr. p. 38]. A delinquency occurred under the terms of said notes and trust deeds and the appellant gave notice of default and scheduled a sale of the real property for October 31, 1947.

Prior to the date set for the sale, the debtors filed their petitions under Chapter XI of the Bankruptcy Act seeking an arrangement with their creditors. Upon order to show cause proceedings commenced by the debtor, Judd Bradley, and upon the taking of evidence and the appointment of an appraiser and a receiver and upon their representations, and after determining that there was a marketable equity in the said real property over and above the amount owing to the appellant, the referee made an

order restraining foreclosure of the trust deeds to permit the debtors to effect their plan of arrangement with their creditors. No review was taken from this order and it is final.

At the time originally scheduled for the foreclosure sale there was a crop of oranges on the trees. This crop was picked and sold by the receiver commencing about November 15, 1947. When it later appeared that the debtors could not carry through their plan of arrangement, they were adjudicated to be bankrupts and a further order was made permitting the foreclosure [Tr. p. 22]. The sale was made on January 7, 1948. At this time the oranges had been removed from the trees and the sale resulted in a deficiency in excess of the amount for which the receiver had sold the crop.

Upon order to show cause proceedings commenced by the receiver, the referee determined that the appellant had no interest in the orange crop which was harvested and sold prior to the foreclosure sale. He made extensive findings of fact and conclusions of law [Tr. pp. 36 and 50] which the District Court affirmed without opinion [Tr. p. 56].

The Question of Law.

The only question is whether the appellant has any interest in the crop which was harvested prior to foreclosure of his deeds of trust and subsequent to the issuance by the bankruptcy court of an order restraining the foreclosure, of which order no review was sought.

Argument.

The attention of the court is invited to the fact that there is no crop mortgage existing in favor of the appellant to support his claim. In fact, a mortgage upon this crop existing in favor of Raymond M. Anderson and El-nora Anderson was set aside as a preference voidable under Section 60 of the Bankruptcy Act (11 U. S. C. Section 96) and the lien of that crop mortgage was ordered preserved for the benefit of the creditors of the estate [Tr. p. 42]. Nor does the fact that appellant's trust deeds included "rents, issues and profits" entitle him to the crop growing upon the realty as against the trustor or as against the holder of a subsequent crop mortgage.

Bank of America v. Bank of Amador County
(1933), 135 Cal. App. 714, 28 P. 2d 86.

It is well established that the security interest passing to the beneficiary of a deed of trust conveying real property together with the rents, issues and profits thereof is in substance no different than that passing to a mortgagee by a real property mortgage.

Kinnison v. Guaranty Liquidating Corporation
(1941), 18 Cal. 2d 256, 115 P. 2d 45.

It is also settled that a mortgagor may sell crops as against his mortgagee and that the mortgagee has no right to the crops until foreclosure and sale.

Bank of Woodland v. Heron (1898), 120 Cal. 614,
52 Pac. 1006.

It is submitted that the same rule governs in the case of trust deeds.

Appellant contends that to deprive him of the proceeds of the sale of the crop would be inequitable. To the contrary. There has been no showing that this crop was part of appellant's security. He took no crop mortgage at any time. There has been no showing that he relied upon the existence of a marketable crop in extending credit to the bankrupt. Only foreclosure at the moment the crop was ripe for picking—a pure, unadulterated windfall—would give him this added security.

Although appellant filed an objection to the restraint against foreclosure [Tr. p. 18, *et seq.*] and a motion to vacate the restraining order [Tr. p. 21, *et seq.*] it is noticeable and conspicuous that nowhere in either the affidavit and objections to restraint against foreclosure, nor the motion to vacate this restraining order, did this appellant demand that the crops growing on the real property involved therein, nor the proceeds of the sale thereof be impounded, sequestered or held for appellant's benefit as additional security.

Attention is also invited to the fact that appellant's deeds of trust were of the purchase money variety [Tr. p. 37]. It is a fair inference that this crop of oranges was produced as a result of credit extended by the Andersons and other unsecured creditors rather than by appellant.

At the foot of page 5 of his opening brief, appellant states that "The title to crops growing on land subject to a Deed of Trust relates back to the date of the giving of the Deed of Trust." This statement is not supported by

either of the two cases cited, neither of which involved title to crops. It is directly opposed to the proposition previously discussed that the trustor may sell these crops prior to foreclosure and may give a crop mortgage upon them.

At page 6, appellant argues that the "Indirect Method of Bankruptcy" should not be invoked to achieve results "Not Within the Direct Power of the Debtor." This argument ignores the many powers conferred upon a trustee in bankruptcy which are not possessed by the debtor or the bankrupt himself. For instance, see Sections 60, 67, 70c and 70e of the Bankruptcy Act (11 U. S. C. Sections 96, 107, 110c and 110e).

Appellant's real complaint seems to be that there was an abuse of discretion by the referee in issuing the original restraining order. At page 7 he says, "The end purpose of such an order could allow successive crops to be harvested and sold until such time as sufficient funds have been realized to pay off all the unsecured creditors in full, thereby, in effect, making a secured creditor pay unsecured creditors." This is a chimerical fear. Such action clearly would be an abuse of discretion which would not be tolerated by our appellate courts. No such abuse is here alleged. Upon the question whether the restraining order should issue, the appellant had his day in court. If there were any abuse of discretion or other judicial error at that time, it is submitted that appellant has waived it by his failure to seek a review of that order.

Conclusion.

Prior to foreclosure, the appellant had no right to the crop in question. At best, he had only a potential right which was postponed and never accrued. He had no right to sell on October 31, 1947, because restrained by the court, and he had no right to the crop as of the date of actual foreclosure because on that date the crop was no longer part of the security. For over fifty years, the Bankruptcy Act has been part of the organic law of the land and the possible effects thereof must be borne in mind by all those engaging in commercial transactions.

It is respectfully submitted that the judgment of the District Court should be affirmed.

Respectfully submitted,

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